JCPenney

1985 Annual Report

"This year, in conjunction with the centennial of the Statue of Liberty, we pay special tribute to our nation's and our Company's proud heritage. . . ."

JCPenney Celebrates American Style

JCPenney

JCPenney Celebrates American Style

"The genius of America is in doing things—making things."
—JAMES CASH PENNEY

Since 1902, JCPenney has been part of the fabric of this country, buying from and selling to Americans of diverse ethnic backgrounds and from all walks of life. This year, in conjunction with the centennial of the Statue of Liberty, we pay special tribute to our nation's and our Company's proud heritage. Come May, our stores from coast to coast will roll out an exciting eight-week merchandising and public relations event called "JCPenney Celebrates American Style."

Taking our cue from this promotion, our Report to you this year presents a selection of photographs from an American family album circa 1986. What you'll see are glimpses of a young married couple's busy, active lifestyle, with accents on family, career, and home, and with merchandise to match the mood and the occasion by JCPenney.

Having ventured abroad in the past two years—to Italy and Britain—to bring exciting fashions and a sense of theater to our JCPenney department stores, we are, you might say, rediscovering the feeling that there's no place like home.

J.C. Penney Company, Inc.
1985 Annual Report

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This is JCPenney

JCPenney is a major retailer, with stores in all 50 states, Puerto Rico, and Belgium. The dominant portion of the Company's business consists of providing merchandise and services to consumers through stores, including catalog operations. The Company markets family apparel, home furnishings, leisure lines, drug store merchandise, and insurance.

Annual Meeting

Our Annual Meeting of Stockholders will be held at 10 A.M., Monday, May 19, 1986, at the Sheraton Crystal City Hotel in Arlington, Virginia. You are cordially invited to attend. A proxy statement, including a request for proxies, will be mailed to stockholders on or about April 10, 1986.

To Our Stockholders:

For JCPenney, 1985 produced both challenges and accomplishments in the implementation of our repositioning strategies. Sales for the year reached a new high of $13.7 billion, rising approximately $300 million. The Company's net income amounted to $397 million, 8.6 per cent below the $435 million earned in 1984. Earnings per share were $5.31, as compared with $5.81 in the prior year. Earnings of our retail divisions totaled $386 million versus $407 million in 1984.

The year got off to a slow start. A sluggish sales pace coupled with some imbalance in our inventory led to additional markdowns and resulted in a decline in retail net income of about 34 per cent in the first half. Prompt clearance activity and modest adjustments in pricing strategies and merchandise assortments saw a reversal in the third quarter, when retail income was about equal to the same period of the prior year.

In the fourth quarter, our performance improved dramatically. Inventories were brought in line with fresh, seasonal merchandise, sales gained momentum, and personnel related costs and advertising expense were tightly controlled. We expect this improvement to continue into 1986 as we maintain our cost control efforts and closely monitor the levels of inventory.

Capital expenditures amounted to $426 million in 1985, compared with $505 million in 1984. Approximately the same amount has been allocated for capital expenditures in 1986 as in the prior year.

Chairman of the board William R. Howell at the Bayshore, Long Island store in the suburban New York area. This store, which was modernized in 1983, is among those that have consistently received the Chairman's Award of Excellence in recognition of their meeting return on equity objectives. The women's sportswear department, seen here, was cited for superior performance in the Company's 1985 National Recognition and Reward Program.

In addition to Mr. Howell, the Office of the Chairman includes Robert B. Gill, David F. Miller, Ralph B. Henderson, and Thomas J. Lyons.

Their Royal Highnesses, The Prince and Princess of Wales, seen at left, at the JCPenney store in Springfield, Virginia. (Top) Escorted on a store tour by chairman of the board William R. Howell and David F. Miller, president of JCPenney stores and catalog. (Bottom, right) Greeted by, among others, (left to right) Frank J. Michela, store manager; William D. Striegl, district manager; A. Scott Frahlich, senior vice president and director of JCPenney stores; and John A. McConville, senior vice president and director of merchandise. The occasion for the historic visit during the fall was our Company's grand-scale "Best of Britain" merchandise event celebrating the culture and commerce of Great Britain. This royal visit received extensive worldwide coverage by the media, conveying our repositioning message to consumers in a very exciting manner.

Financial Highlights (In millions except per share data)

For the Year	1985	1984	1983
Sales	**$13,747**	$13,451	$12,078
Sales of JCPenney stores and catalog	**$12,634**	$12,372	$11,033
Per cent increase from prior year	**2.1**	12.1	6.5
Retail income	**$ 386**	$ 407	$ 441
Per cent increase (decrease) from prior year	**(5.1)**	(7.7)	9.0
Per cent of sales	**2.8**	3.0	3.7
Net income	**$ 397**	$ 435	$ 467
Per cent of stockholders' equity	**10.4**	12.2	14.5
Net income per share	**$ 5.31**	$ 5.81	$ 6.25
Dividends per share	**$ 2.36**	$ 2.36	$ 2.16
Capital expenditures	**$ 426**	$ 505	$ 443

The Company opened 41 JCPenney stores during 1985, of which 34 were relocations of existing stores. Aside from the relocations, a total of 95 stores—mostly smaller units—were closed. Gross selling space for all JCPenney stores decreased slightly, with the total at year end amounting to 115.5 million square feet.

We plan in 1986 to open 20 department stores in regional shopping centers and 25 geographic stores in smaller markets as well as 25 drug stores and 45 catalog sales centers. JCPenney store space, net of closings, is expected to be approximately the same as in 1985.

Since the modernization program began, all of our approximately 550 department stores have been either modernized or, as an interim step, updated with a more contemporary look. In addition, there has been extensive refurbishing of several hundred stores in smaller markets. Stores accounting for one-third of our department store sales volume have been modernized to date, and we expect these stores to contribute significantly to future profits.

A broad range of programs and strategies in the areas of space productivity, merchandise, presentation, advertising, and customer service support our repositioning program,

Vice chairman of the board Robert B. Gill is a frequent visitor to the nation's capital. As the senior officer responsible for government relations, he regularly participates in Congressional hearings and meets with the Congressional leadership and administration officials concerning issues that affect the Company. Mr. Gill also oversees finance, personnel, auditing, and public affairs and Company communications.

which commenced three years ago. These programs have been effective in improving the performance of our stores, and they are continually undergoing review, enhancement, and refinement.

In positioning our merchandise mix, our programs are responsive to the needs of individual markets. Our strategy aims at achieving a balance of appropriately priced good, better, and best levels of merchandise in each category to provide the necessary selection for all our customers. It also aims at a balanced mix of private label, national brands, and designer labels suitable for each merchandise area to further enhance this selection.

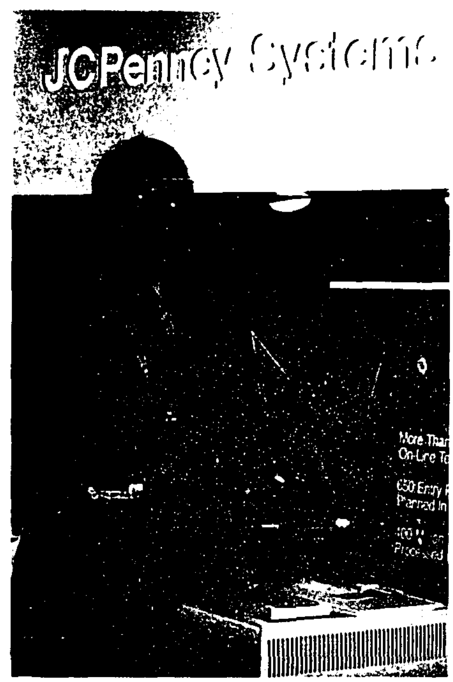
New assortment planning procedures permit stores to adjust to competition and to tailor their merchandise mix to customers' needs, reflecting differences in climate, lifestyle, and personal preference. The procedures involve a regular series of merchandise meetings broadcast on our satellite television network from New York to 160 of our facilities around the country. During these broadcasts, buyers show merchandise offerings to store associates who plan assortments suitable for their stores' customers, primarily in the fashion area.

Studies by an independent research organization show a significant increase since our repositioning began in JCPenney's share of the total soft goods market, including women's, men's, and children's apparel and soft home furnishings. Particularly notable are gains in such merchandise categories as women's sportswear, dresses, accessories, and lingerie; men's sportswear, dress shirts, ties, and leather goods; boys' and girls' apparel; and window coverings and bedding and bath merchandise. Our own studies demonstrate that customers' perceptions of JCPenney have also improved as a result of our repositioning efforts in such key areas as store ambiance, fashionability of apparel offerings, and the friendliness and helpfulness of our salespeople.

JCPenney's efforts to maintain a competitive edge in the areas of technology and communications are ongoing. A long-range program to install electronic point of sale (POS) systems in all JCPenney stores was successfully completed in 1985. The POS system, which provides data capture, price lookup, and credit authorization, connects stores with other JCPenney facilities in a nationwide electronic communications network. This technology contributes to greater effectiveness in the areas of customer service, inventory management, associate productivity, and information management.

A new catalog telephone center scheduled for opening in early 1986 will complete our nationwide network of 14 on-line telephone centers. These centers, which utilize the Company's extensive voice and electronic communications network, greatly facilitate order placement by customers through advanced technology, toll-free numbers, and trained order takers. Customer response has been extremely favorable.

Our investment in advanced electronic communications network technology has been primarily for the benefit of JCPenney's retailing operations. However, this also has allowed



Executive vice president Ralph B. Henderson at the JCPenney Systems Services exhibit booth at the National Retail Merchants Association annual convention in New York City. Our Systems Services subsidiary, which Mr. Henderson oversees, markets use of the Company's nationwide electronic communications network to other companies. The industries currently being served by Systems Services are petroleum, retailing, and banking. Mr. Henderson's responsibilities include systems and data processing, distribution, planning and research, real estate, construction, and corporate services.

David F Miller, president of JCPenney stores and catalog, with Their Royal Highnesses, The Duke and Duchess of Kent, at a special press reception at our corporate offices in New York City on October 15. This was followed by visits to our Rockaway, New Jersey, and Glendale Galleria, Los Angeles, stores, thus officially launching our "Best of Britain" event in some 500 JCPenney stores nationwide. The promotion featured fashion apparel and accessories of British origin or design.

us to enter new businesses which market our capabilities to other companies. Such businesses as JCPenney Systems Services, JCPenney Credit Services, JCPenney Communications, and a telephone reservations service targeted primarily at airlines are currently marketing both technology and their years of experience to other companies.

During 1985, we elected Clifton C. Garvin, Jr., chairman and chief executive officer of Exxon Corporation, a director of the Company.

Walter J. Neppl, former JCPenney president and vice chairman of the board, retired from our board of directors in 1985. Marshall S. Armstrong, visiting professor of accounting at Butler University and chairman emeritus of the Financial Accounting Standards Board, and Oscar L. Dunn, chairman and chief executive officer of Zurn Industries, Inc., also retired as directors. We wish to express our appreciation to Messrs. Neppl, Armstrong, and Dunn for their outstanding service to JCPenney.

We also wish to recognize the outstanding service rendered by Wilburn L. Morris, senior vice president and director of JCPenney stores, who retired since our last Report.

As we move into 1986, we are confident of the direction of our repositioning and our ability to achieve it. Programs and strategies are undergoing refinements and enhancements on an ongoing basis to strengthen our ability to satisfy existing customers and to attract new ones.

Through our repositioning efforts, we are making an investment in the future of JCPenney. We believe that we are well situated to leverage our sales increases into a higher profitability in the years ahead.

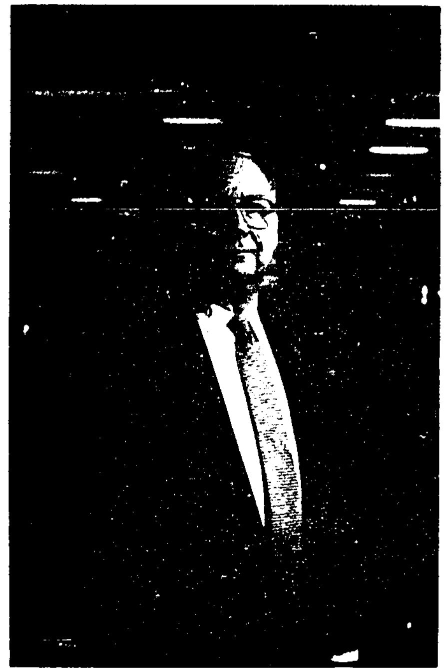
We take this opportunity to express our sincere appreciation to all of our dedicated associates whose efforts have contributed to a challenging and productive year. We also thank our customers, suppliers, and stockholders for their continued support and loyalty.

Warmest regards,

W R Howell

William R. Howell
Chairman of the Board

March 25, 1986



Executive vice president Thomas J. Lyons at the mall entrance to our Thrift Drug store in Cedar Knolls, New Jersey. Thrift Drug, which Mr. Lyons oversees, celebrated its golden anniversary in 1985. It is now the fourteenth largest drug store chain in the country with some 375 stores located primarily in convenience shopping centers. Mr. Lyons also has responsibility for credit and consumer banking services, insurance, and European operations.

JCPenney

Statement of Income (In millions except per share data)

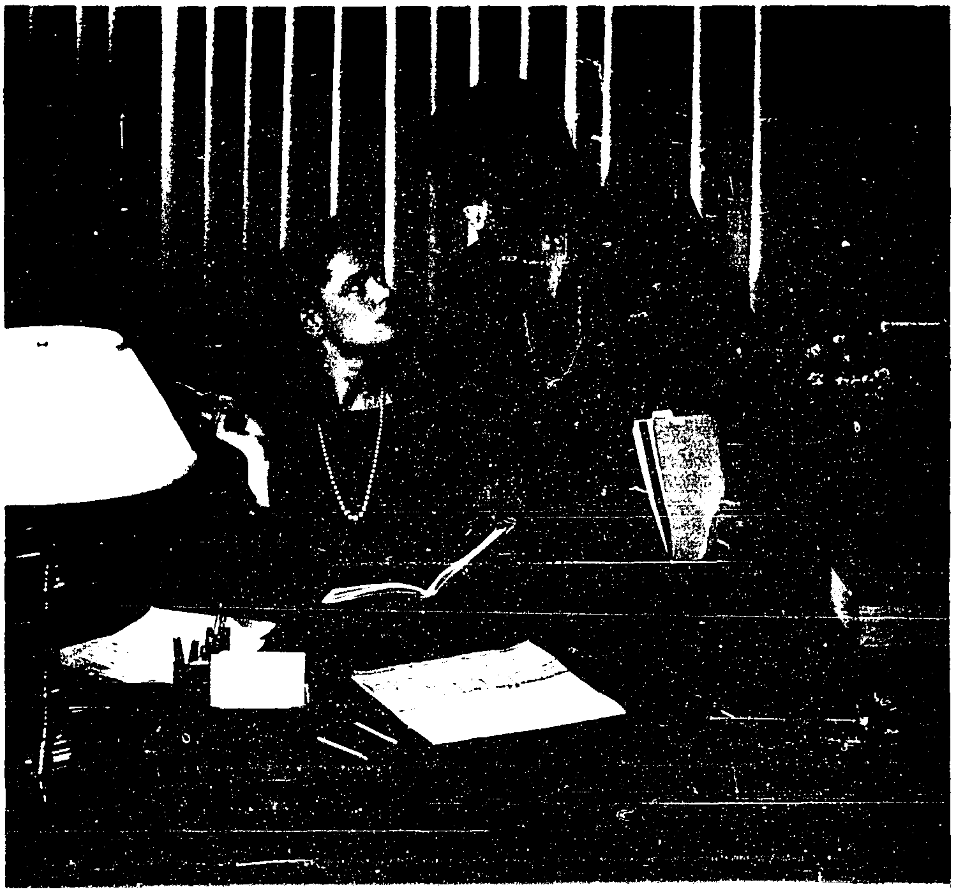
J C Penney Company, Inc and Consolidated Subsidiaries

For the Year	1985	1984	1983
Sales	**$13,747**	$13,451	$12,078
Costs and expenses			
Cost of goods sold, occupancy, buying, and warehousing costs	**9,240**	9,030	8,053
Selling, general, and administrative expenses	**3,454**	3,374	2,973
Interest expense, net	**370**	350	266
Total costs and expenses	**13,064**	12,754	11,292
Retail income before income taxes	**683**	697	786
Income taxes	**297**	290	345
Retail income	**386**	407	441
Income of unconsolidated subsidiaries	**11**	28	26
Net income	**$ 397**	$ 435	$ 467
Net income per share	**$ 5.31**	$ 5.81	$ 6.25

Statement of Reinvested Earnings (In millions)

	1985	1984	1983
Reinvested earnings at beginning of year	**$2,890**	$2,640	$2,336
Net income	**397**	435	467
Unrealized change in market value of equity securities	**9**	(7)	1
Foreign currency translation adjustment	**2**	(3)	(4)
Dividends	**(176)**	(175)	(160)
Reinvested earnings at end of year	**$3,122**	$2,890	$2,640

See Summary of Accounting Policies on page 11 and 1985 Financial Review on pages 12 through 27.



One has to look no further than the Bureau of Labor Statistics to understand the importance of the working mother to JCPenney. In 1985, the number of employed mothers shot up 765,000 to 18.2 million. This was paralleled by a rise in median family wage and salary earnings nationwide.

To aid these women in organizing their busy lives, JCPenney offers an increasing number of coordinated lines of separates that add flexibility to a wardrobe while assuring the wearer she can be appropriately dressed from an early morning business breakfast right through to dinner and the theater. Shown here are two such outfits: on the left, an updated two piece dress with floral jacket, and on the right, a grey wool-blend skirt and jacket, worn over a classic blouse in cerise.

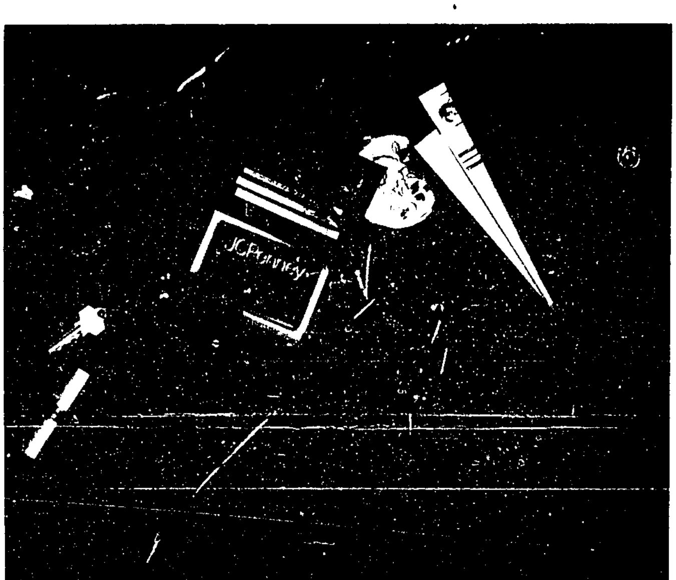
Balance Sheet (In millions)

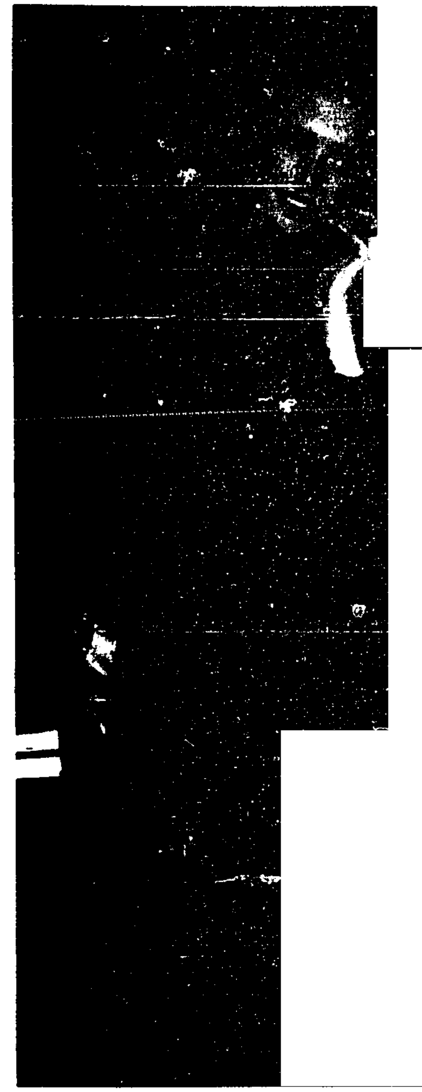
J C Penney Company, Inc and Consolidated Subsidiaries

Assets	1985	1984	1983
Current assets			
Cash and short term investments of $136, $161, and $214	**$ 158**	$ 187	$ 238
Receivables, net	**4,504**	4,019	3,673
Merchandise inventories	**2,298**	2,383	1,993
Prepaid expenses	**117**	134	115
Total current assets	**7,077**	6,723	6,019
Investment in and advances to unconsolidated subsidiaries	**372**	299	259
Properties, net of accumulated depreciation and amortization of $1,151, $1,015, and $897	**2,812**	2,608	2,358
Other assets	**261**	163	224
	$10,522	$9,793	$8,860

Liabilities and Stockholders' Equity	1985	1984	1983
Current liabilities			
Accounts payable and accrued expenses	**$ 1,282**	$1,145	$1,268
Short term debt	**740**	802	609
Current maturities of long term debt	**—**	125	100
Deferred taxes, principally installment sales	**701**	628	515
Total current liabilities	**2,723**	2,700	2,492
Long term debt	**3,099**	2,847	2,440
Deferred taxes, principally depreciation	**649**	434	369
Stockholders' equity			
Common stock, par value 50¢: Authorized, 500 million shares—issued, 75, 74, and 74 million shares	**929**	922	919
Reinvested earnings	**3,122**	2,890	2,640
Total stockholders' equity	**4,051**	3,812	3,559
	$10,522	$9,793	$8,860

See Summary of Accounting Policies on page 11 and 1985 Financial Review on pages 12 through 27.





A versatile, all-wool coat is a staple of any career woman's wardrobe. This coat, with a fashionable shawl collar, will be available for Fall 1986 in several of the new season's colors.

Accessories is one area of the retailing business in which there's been lots of action. It's also an area in which JCPenney has increased its market share in the last year. One of the reasons for this gain relates to the breadth, quality, and fashionability of the merchandise we offer. Shown here is a signature shoulder bag done in embossed vinyl and trimmed with leather. To complete the picture, we show a coordinated selection of leather goods in full grain nude lambskin, embossed with an Aztec pattern.

Statement of Changes in Financial Position (In millions)

J C Penney Company, Inc and Consolidated Subsidiaries

For the Year	1985	1984	1983
Funds generated from operations			
Net income before undistributed income of unconsolidated subsidiaries	**$ 386**	$ 407	$ 441
Depreciation and amortization	**212**	198	153
Deferred taxes, principally depreciation	**215**	65	101
Amortization of original issue discount	**39**	35	30
	852	705	725
Deferred taxes, principally installment sales	**73**	113	11
Funds generated from operations	**925**	818	736
Operating and investing activities			
Increase in receivables	**485**	346	49
Increase (decrease) in inventories	**(85)**	390	399
Capital expenditures	**426**	505	443
Dividends	**176**	175	160
(Increase) decrease in accounts payable and accrued expenses	**(137)**	123	(74)
Investments and other, net	**122**	(77)	20
Funds used	**987**	1,462	997
External funds required	**$ 62**	$ 644	$ 261
Financing activities			
Increase (decrease) in short term debt	**$ (62)**	$ 193	$ (51)
Decrease in cash and short term investments	**29**	51	96
Increase (decrease) in short term debt, net	**(33)**	244	45
Increase in long term debt	**313**	497	289
Retirement of long term debt including payments of current maturities	**(225)**	(100)	(100)
Common stock issued	**7**	3	27
Total	**$ 62**	$ 644	$ 261

See Summary of Accounting Policies on page 11 and 1985 Financial Review on pages 12 through 27.

Company Statement on Financial Information

The Company is responsible for the information presented in this Annual Report. The financial statements have been prepared in accordance with generally accepted accounting principles and are considered to present fairly in all material respects the Company's results of operations, financial position, and changes in financial position. Certain amounts included in the financial statements are estimated, based on currently available information and judgment of the outcome of future conditions and circumstances. Financial information elsewhere in this Annual Report is consistent with that in the financial statements.

The Company's system of internal accounting controls is supported by written policies and procedures and supplemented by a staff of internal auditors. This system is designed to provide reasonable assurance, at suitable cost, that assets are safeguarded and that transactions are executed in accordance with appropriate authorization and are recorded and reported properly. The system is continually reviewed, evaluated, and, where appropriate, modified to accommodate current conditions. Emphasis is placed on the careful selection, training, and development of professional managers.

An organizational alignment that is premised upon appropriate delegation of authority and division of responsibility is fundamental to this system. Communication programs are aimed at assuring that established policies and procedures are disseminated and understood throughout the Company.

The financial statements have been examined by independent certified public accountants whose report appears on page 11.

The Audit Committee of the Board of Directors is composed solely of directors who are not officers or employees of the Company. The Audit Committee is responsible for recommending to the Board the engagement of the independent certified public accountants for the purpose of conducting the annual examination of the Company's financial statements. Company personnel, including internal auditors, and the independent certified public accountants meet periodically with the Audit Committee to review financial statements and discuss auditing and financial reporting matters.

Always in fashion are men's suits sporting labels that stand for good taste. Two such, seen on the opposite page, are: the Stafford label, as seen on the model on the left, and Daks, which was introduced in our stores with our "Best of Britain" promotion last year.

In men's haberdashery, the yellow tie became ubiquitous in 1985 as thousands of men discovered how great it looks with a blue shirt or even one in pink, which is one of the hot colors for Spring.

JCPenney

Management's Discussion and Analysis of Results of Operations and Financial Position

Results of operations (Per cent of sales)	**1985**	1984	1983
Sales, per cent increase	**2.2**	11.4	5.8
Gross margin	**32.8**	32.9	33.3
Selling, general, and administrative expenses	**25.1**	25.1	24.6
Interest expense, net	**2.7**	2.6	2.2
Retail income	**2.8**	3.0	3.7

Retail income was $386 million in 1985, compared with $407 million in 1984 and $441 million in 1983. The decline in 1985 was due principally to the impact of the LIFO method of inventory valuation which resulted in an after tax charge of $8 million in 1985 and credits of $29 million in 1984 and $22 million in 1983. Retail income on a FIFO basis, which does not consider the effects of LIFO, increased 4.3 per cent in 1985 to $394 million from $378 million in 1984 but declined from $419 million in 1983. The decline in retail income in 1984 was due to heavy markdowns.

Net income was $397 million in 1985, compared with $435 million in 1984 and $467 million in 1983. Net income declined in 1985 by $38 million, or 8.6 per cent. In addition to the effect of LIFO, the net income of unconsolidated subsidiaries decreased by $17 million in 1985 as shown on pages 15 and 18. This decrease was principally attributable to higher underwriting losses in our casualty insurance operation. Net income per share, based on 75 million weighted average number of shares, was $5.31, $5.81, and $6.25 in 1985, 1984, and 1983, respectively. In the five years ended January 25, 1986, income from continuing operations increased at a compound annual rate of 7.0 per cent.

Gross margin, as a per cent of sales, decreased slightly in 1985. Markdowns were reduced as inventories were well controlled. However, the negative impact of LIFO resulted in the decline. In 1984, gross margin declined due to heavy markdowns. Gross margin improved in 1983 as a result of an increase in markup due to changes to a more fashionable merchandise mix. The impact of the LIFO method of inventory valuation resulted in a pre-tax charge of $16 million in 1985 and credits of $57 million and $44 million in 1984 and 1983, respectively. The 1985 LIFO charge was due to higher general merchandise inflation and a leveling off of markup. The LIFO credits in 1984 and 1983 resulted from a combination of lower inflation and higher markup from changes in merchandise mix.

Selling, general, and administrative expenses rose 2.4 per cent in 1985, as compared with 13.5 per cent and 7.7 per cent increases in 1984 and 1983, respectively. Personnel related costs and advertising expense were tightly controlled. In 1984 and 1983, the increases were attributed to management's efforts to communicate the Company's repositioning to consumers through improved customer service, increased advertising, and promotional events.

Interest expense was $370 million in 1985, compared with $350 million in 1984 and $266 million in 1983. The rate of increase in interest expense declined in 1985 as compared with the previous year, reflecting lower levels of inventory. Higher borrowing levels to finance increased inventories and capital expenditures in connection with the store modernization program accounted for the 1984 and 1983 increases.

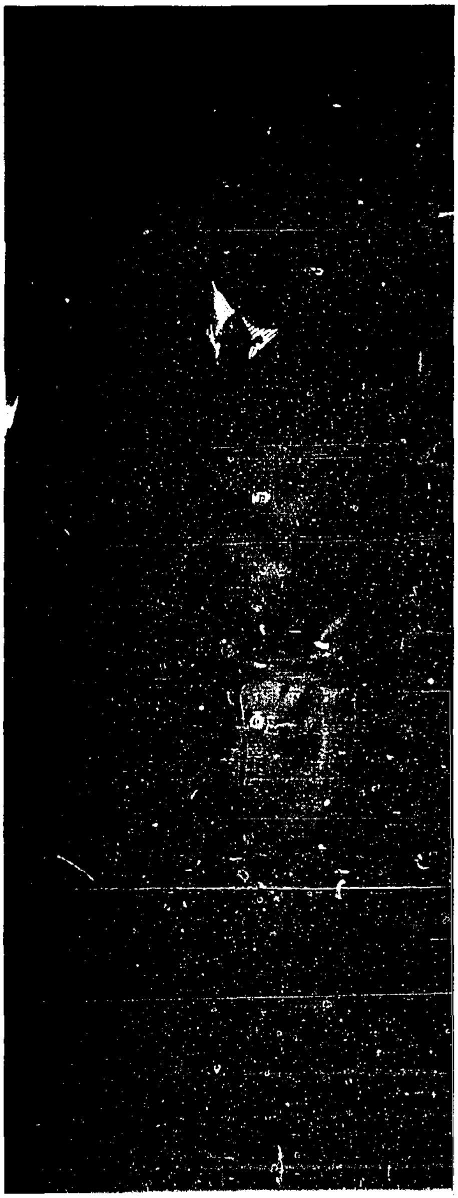
Financial Position. Funds generated from operations increased to $925 million in 1985 from $818 million in 1984, and $736 million in 1983. Although net income was lower in 1985, noncash charges, principally deferred taxes, increased substantially during the year. The principal portion of funds required to finance the Company's business activities continued to be provided by operations and have averaged approximately 70 per cent during the past five years.

Receivables increased $485 million in 1985, as a result of an increase of 12.1 per cent in customer receivables, reflecting higher credit sales. The proportion of credit sales to eligible sales has steadily increased in recent years as the Company's merchandise mix has changed in conjunction with the Company's repositioning strategies.

Merchandise inventories decreased $85 million, or 3.6 per cent in 1985 compared with significant increases in 1984 and 1983. With lower levels of inventories, funds generated from operations in 1985 were almost sufficient to cover operating and investing activities, including dividends to stockholders. During 1984 and 1983, the external funds required were financed principally through the issuance of long term debt.

The Company anticipates that the major portion of funds required during the next few years to finance customer receivables, inventories, and expansion and modernization, and to repay amounts borrowed, will continue to be provided from operations. Additional funds required will be financed with either long term debt or short term debt, including commercial paper and master notes issued by the Company's wholly-owned finance subsidiary, J.C. Penney Financial Corporation. The Company will continue to review all uses of funds to maximize financial returns and maintain financial flexibility.

Additional Information. For additional discussion and analysis of 1985, see the 1985 Financial Review on pages 12 through 27. For required information as to the impact of inflation on financial data, see page 31.



Summary of Accounting Policies

The dominant portion of JCPenney's business consists of selling merchandise and services to consumers through stores, including catalog operations.

Basis of Consolidation. The accounts of J.C. Penney Financial Corporation (Financial), a wholly-owned subsidiary whose primary activity is to finance the Company's operations, are, for the first time, included in the Company's consolidated financial statements in order to more appropriately reflect the financial structure of the Company. Prior to 1985, Financial was presented as an unconsolidated subsidiary accounted for by the equity method and its income before income taxes was included as a reduction of interest expense. This change had no effect on the Company's Statement of Income; however, the Balance Sheet and the Statement of Changes in Financial Position have been retroactively restated. For a more detailed description of Financial, refer to its 1985 annual report, which is available upon request.

The consolidated financial statements present the results of J.C. Penney Company, Inc. and its subsidiaries except for the insurance operations, the bank, and real estate development operations, which are accounted for by the equity method. The combined income of these unconsolidated operations is included as a single item in the Statement of Income. Intercompany items and transactions have been eliminated in consolidation.

Definition of Fiscal Year. JCPenney's fiscal year ends on the last Saturday in January. Fiscal year 1985 ended January 25, 1986, 1984 ended January 26, 1985, and 1983 ended January 28, 1984. Each year is comprised of 52 weeks. The accounts of J.C. Penney Life Insurance Company, J.C. Penney Casualty Insurance Company, and the JCPenney National Bank are on a calendar year basis.

Sales. Sales include merchandise and services, net of returns, and exclude sales and value added taxes.

Finance Charge Revenue. Finance charge revenue arising from customer accounts receivable is treated as a reduction of selling, general, and administrative expenses in the Statement of Income.

Merchandise Inventories. Substantially all merchandise inventories are valued at the lower of cost (last-in, first-out) or market, determined by the retail method.

Depreciation. The cost of buildings and equipment is depreciated on a straight line basis over the estimated useful lives of the assets. The principal annual rates of depreciation are 2 per cent for buildings, 5 per cent for warehouse fixtures and equipment, and 10 per cent for selling fixtures and equipment. Improvements to leased premises are amortized on a straight line basis over the expected term of the lease or their useful lives, whichever is shorter.

Income Taxes. JCPenney uses the "flow through" method whereby income taxes are reduced currently for the amounts of investment tax credits. Deferred taxes consist principally of deferred gross profit on the balances due on installment sales, accelerated depreciation, and accounting for leases.

Deferred Charges. Expenses associated with the opening of new stores are written off in the year of store opening, except those of stores opened in January, which are written off in the following fiscal year. Catalog preparation and printing costs are written off over the estimated productive lives of the catalogs, not to exceed six months.

JCPenney Financial Services' policy acquisition costs, which are primarily marketing and underwriting expenses related to generating new insurance policies, are deferred and, subject to recoverability, are amortized over the expected premium paying period of the related policies. The maximum period was 15 years for life and health policies and five years for automobile and homeowners policies.

Pension Cost. The cost of pension benefits has been determined by the projected unit credit actuarial method. The difference between pension fund assets and obligations is amortized over ten years.

Accountants' Report

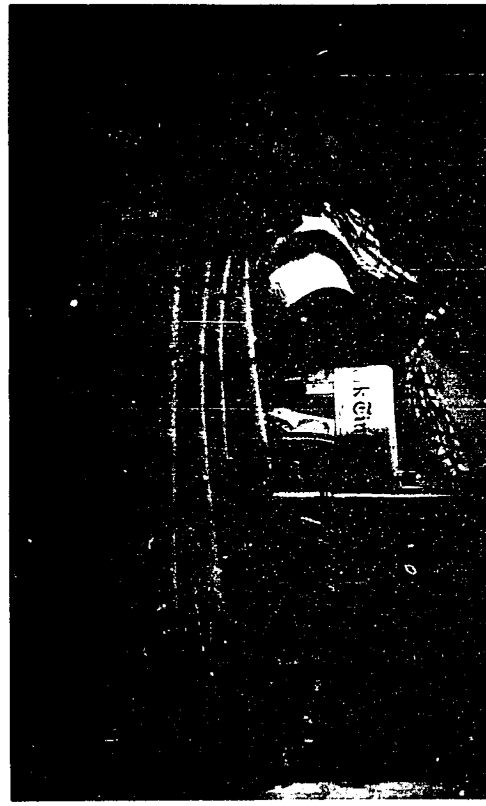
To the Stockholders and Board of Directors of J.C. Penney Company, Inc.

We have examined the balance sheet of J.C. Penney Company, Inc. and Consolidated Subsidiaries as of January 25, 1986, January 26, 1985, and January 28, 1984, and the related statements of income, reinvested earnings, and changes in financial position for the years then ended. Our examinations were made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the aforementioned financial statements present fairly the financial position of J.C. Penney Company, Inc. and Consolidated Subsidiaries at January 25, 1986, January 26, 1985, and January 28, 1984, and the results of their operations and the changes in their financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis after restatement for the change, with which we concur, in the basis of consolidation as it relates to J.C. Penney Financial Corporation as described in the Summary of Accounting Policies.

345 Park Avenue, New York, N.Y.
February 25, 1986

Peat, Marwick, Mitchell & Co.



Daks does it all for the businessman. The trench coat with zipout lining is the ideal travel coat and looks equally smart over business suit, jeans, or black tie. Coordinating cap and umbrella and fine leather accessories complete the well put-together look.

1985 Financial Review

Sales in 1985 were $13,747 million, an increase of 2.2 per cent over $13,451 million in 1984.

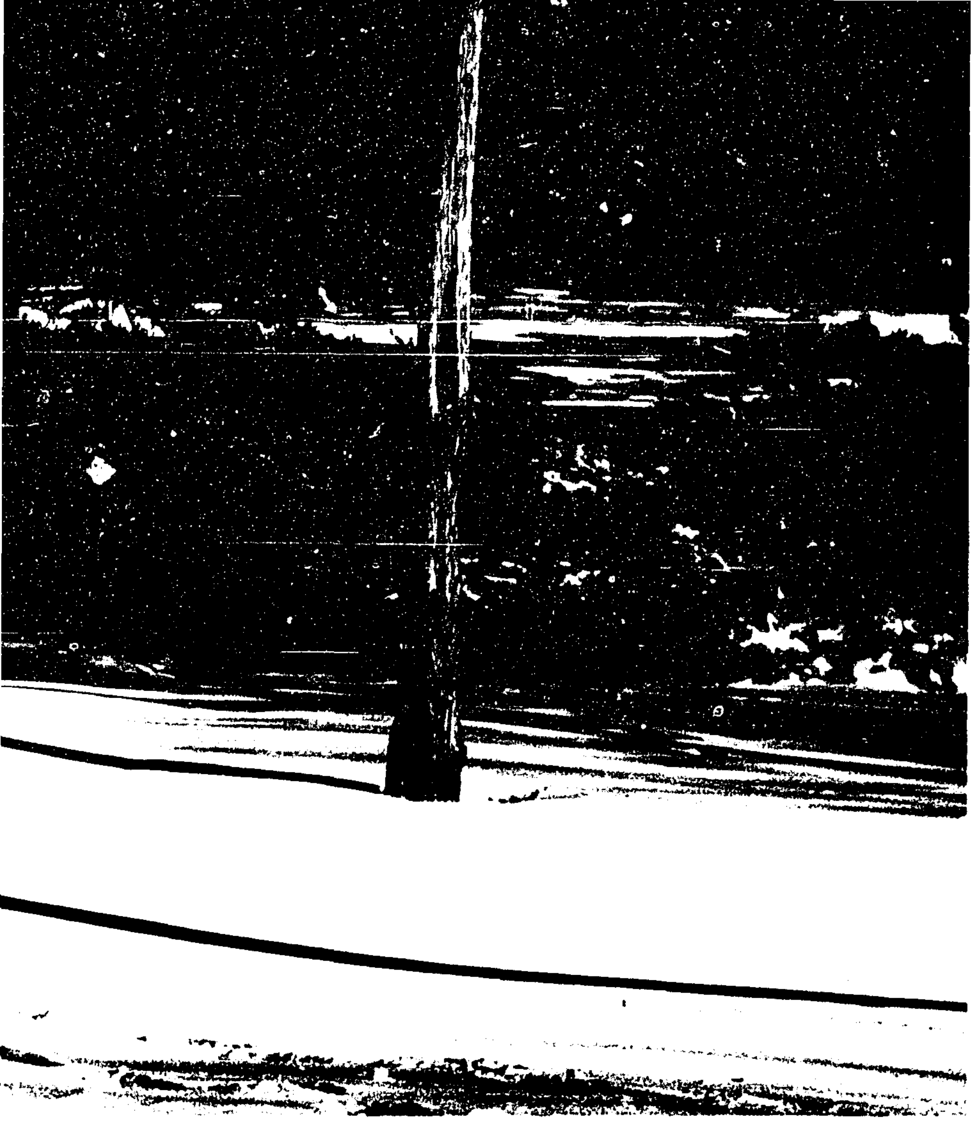
Sales (In millions)	**1985**	Per cent increase 1985 vs. 1984: All units	Per cent increase 1985 vs. 1984: Comparative units	1984	Per cent increase 1984 vs. 1983: All units	Per cent increase 1984 vs. 1983: Comparative units	1983
JCPenney stores	**$12,165**	2.1	1.5	$11,913	12.1	11.4	$10,625
Catalog	**2,000**	3.7	5.5	1,928	5.3	5.6	1,831
Intracompany elimination	**(1,531)**	n/a	n/a	(1,469)	n/a	n/a	(1,423)
Total JCPenney stores and catalog	**12,634**	2.1	1.5	12,372	12.1	11.4	11,033
Other retail operations	**1,113**	3.2	3.2	1,079	3.2	4.1	1,045
Total	**$13,747**	2.2	1.7	$13,451	11.4	10.8	$12,078

Catalog merchandise sold through catalog sales departments located in JCPenney stores is included in the sales of those stores and Catalog. The duplication with respect to these sales is eliminated. Sales of drug stores included in "other retail operations" exclude sales by catalog sales departments in the amounts of $61 million, $58 million, and $54 million, in 1985, 1984, and 1983, respectively. Comparative units are those in operation throughout both the current and prior year. For further analyses of sales, see the discussions that follow and the Five Year Operations Summary on page 29.

If our young father is typical of men aged 25 to 44, he spends 14 or more hours per week on household chores and child care. This, says a recent University of Michigan study, is three hours more than he would have spent back in 1975.

Bundling two packages of boundless energy into JCPenney's colorful winter outerwear may be, however, the only part of this family scene that qualifies as work for Dad, who sports his very up-to-date corduroy jacket and pants, coordinated with a patterned sweater.

And, as for Mom, walking the family dog can be an added pleasure when there's a snap in her outfit as well as in the air.



JCPenney Stores

JCPenney stores' sales (In millions)	1985	Per cent increase (decrease) 1985 vs. 1984: All units	Per cent increase (decrease) 1985 vs. 1984: Comparative units	1984*	Per cent increase (decrease) 1984 vs. 1983: All units	Per cent increase (decrease) 1984 vs. 1983: Comparative units	1983*
Metropolitan markets							
Department stores	**$ 9,524**	3.5	2.5	$ 9,200	13.8	12.2	$ 8,082
Soft line stores	**858**	(3.9)	.8	893	(1.5)	9.3	906
Geographic markets	**1,783**	(2.0)	(3.4)	1,820	11.2	8.2	1,637
Total	**$12,165**	2.1	1.5	$11,913	12.1	11.4	$10,625

**Restated to reflect reclassification of stores.*

Metropolitan market stores are located in metropolitan areas and in some of the larger nonmetropolitan cities. The department stores are situated primarily in premier regional shopping centers, serving the suburbs of these larger markets and offering family apparel, home furnishings, and leisure lines. The soft line stores are in older generation shopping centers and business districts serving the more densely populated, mature suburbs and urban sectors of these markets.

The Company had 566 metropolitan department stores in operation at year end. These stores vary widely in size and average 157 thousand square feet of gross selling space. Sales per square foot of gross selling space were approximately $107 for stores in operation throughout 1985. The Company is continuing its major modernization program, whereby virtually all metropolitan department stores will be modernized. In addition, the Company continues to open new stores as opportunities arise, and will close stores that do not meet performance objectives. During 1985, 14 department stores were opened and 13 were closed.

At year end, the Company had 163 metropolitan soft line stores in operation, averaging 48 thousand square feet of gross selling space. Sales per square foot of gross selling space were approximately $103 for stores in operation throughout 1985. During 1985, no soft line stores were opened and 21 were closed.

Metropolitan market stores' profit increased in 1985 through an improvement in gross margin coupled with tight expense controls. Metropolitan market stores' profit declined in 1984 as a result of increased promotional activity. In 1983, profits increased due to increased sales and an improvement in gross margin.

Geographic market stores are located in nonmetropolitan areas and in satellite towns within metropolitan areas. These stores emphasize family apparel and soft home furnishings. Catalog sales departments located in these stores contribute substantially to sales and profit.

At year end, the Company had 753 geographic market stores in operation, averaging 25 thousand square feet of gross selling space. Sales per square foot of gross selling space were approximately $93 for geographic market stores in operation throughout 1985. During 1985, 27 geographic market stores were opened and 95 were closed. The Company continues to modernize existing stores, expand into new markets, and close unproductive stores.

Geographic market stores' profit increased in 1985 due to higher gross profit and tight expense controls. Geographic market stores' profit declined in 1984 due primarily to increased promotional activity. In 1983, profits increased as a result of higher gross margin.

Catalog

Catalog operations expand the Company's retailing capabilities by offering a wide range of family apparel, home furnishings, and leisure merchandise. Catalog operations serve customers who purchase merchandise which is shipped to catalog sales departments or directly to customers' homes. Catalog sales departments are located in all JCPenney stores, selected drug stores, and in free standing facilities. Orders are generally delivered in 72 hours or less.

The Company publishes two general catalogs: Fall and Winter and Spring and Summer. These are supplemented by Christmas and other seasonal and promotional catalogs.

The operation of catalog's on-line order entry capability available through catalog telephone centers enhances customer service by providing immediate information on merchandise availability and alternative in-stock selections if the customers' initial selections are not currently available. During 1985, 78 per cent of total catalog sales were placed through catalog's on-line telephone centers compared with 47 per cent in 1984. By year end 1985, virtually all orders were placed through telephone centers.

		Per cent increase (decrease) 1985 vs. 1984			Per cent increase (decrease) 1984 vs. 1983		
Catalog sales (In millions)	**1985**	All units	Comparative units	1984*	All units	Comparative units	1983*
JCPenney stores							
Metropolitan markets							
Department stores	**$ 882**	6.2	5.3	$ 830	7.6	5.9	$ 772
Soft line stores	**153**	(1.9)	4.8	156	(5.9)	3.7	166
Geographic markets	**426**	.0	1.6	426	1.4	2.0	420
Other	**539**	4.5	10.8	516	9.1	10.8	473
Total	**$2,000**	3.7	5.5	$1,928	5.3	5.6	$1,831

**Restated to reflect reclassification of stores.*

Catalog's profit declined in 1985 due to continued higher start-up costs associated with the expansion of the on-line telephone centers. Catalog's profit declined in 1984 as a result of moderating sales in the latter part of the year, which resulted in lower gross margin, and start-up costs from the on-line telephone centers. In 1983, profits increased due to higher sales and improved gross margin.

Once it was the stationary bike; now it's the rowing machine that is becoming a favorite way to stay in shape. When not in use, this top-of-the-line model by West Bend folds up for easy storage. Stylish workout clothes not only get some people in the mood but also add a certain seriousness to the pursuit of exercise, so they say.

Surveys show that sales of home fitness equipment are growing by 15 per cent a year, twice as fast as the sales of institutional exercise equipment. JCPenney is participating in this growth with both stores and catalog providing customers with lots of merchandise that can help them stay in shape.

JCPenney

Other Retail Operations

Sales of other retail operations (In millions)	1985	Per cent increase (decrease) 1985 vs. 1984		1984	Per cent increase (decrease) 1984 vs. 1983		1983
		All units	Comparative units		All units	Comparative units	
Drug stores	**$ 641**	8.5	7.3	$ 591	11.1	9.9	$ 532
Belgian operations	**472**	(3.2)	(2.2)	488	(4.9)	(3.4)	513
Total	**$1,113**	3.2	3.2	$1,079	3.2	4.1	$1,045

Drug stores, operating under the name Thrift Drug or The Treasury Drug Center, average 11 thousand square feet of gross selling space and offer typical drug store merchandise, including prescription drugs and health and beauty aid products. During 1985, seven drug stores were opened and two were closed. At year end, the Company operated 374 drug stores.

Drug stores' profit continued at record levels. Profits increased in 1985 as a result of higher sales and improved gross margin. Profits increased in 1984 and 1983 due to higher sales and improved expense control.

Belgian stores, operating under the name Sarma, sell general merchandise, food, and apparel. At year end, there were 53 Sarma stores with an average of 62 thousand square feet of gross selling space. Belgian operations include sales to franchised stores of $283 million in 1985, $294 million in 1984, and $299 million in 1983. At year end, 194 franchised stores were in operation.

Belgian operations recorded small losses in 1985, 1984, and 1983. Net assets were approximately $40 million in each of the last three years.

Unconsolidated Subsidiaries

Investment in and advances to unconsolidated subsidiaries at equity (In millions)	1985	1984	1983
JCPenney Financial Services	**$395**	$341	$306
JCP Realty, Inc.	**(23)**	(42)	(47)
Total	**$372**	$299	$259

JCPenney Financial Services consists principally of the operations of the Company's insurance subsidiaries and JCPenney National Bank, acquired in 1983. The Company's insurance subsidiaries market life and health insurance and automobile and homeowners casualty insurance. In 1985, 11 insurance centers located primarily in JCPenney stores were opened and 46 were closed in markets with low productivity. This brought the total at year end to 199 insurance centers in 26 markets.

The Company's advances and capital contributions to JCPenney Financial Services were $56 million in 1985 and $20 million in both 1984 and 1983.

JCPenney Life Insurance Company, in 1985, reported record net income from operations as a result of increased premiums and favorable claims experience. JCPenney Casualty Insurance Company's loss was substantially higher in 1985 due to higher underwriting losses in the automobile and homeowners insurance business.

Summary of insurance operations (In millions)	Year ended December 31 1985	1984	1983
Premiums earned	**$308**	$248	$211
Investment income	**52**	42	42
Total revenues	**360**	290	253
Benefits, claims, and expenses	**395**	286	229
Income (loss) before income taxes	**(35)**	4	24
Income taxes (benefits)	**(24)**	(18)	3
Net income (loss)	**$ (11)**	$ 22	$ 21
JCPenney Life			
Operations	**$ 23**	$ 22	$ 17
Tax benefit*	**—**	14	—
JCPenney Casualty	**(34)**	(14)	4
Net income (loss)	**$ (11)**	$ 22	$ 21

**The Tax Reform Act of 1984 required life insurance companies to recompute policy reserves for tax purposes in 1984, and provided that deferred taxes on income arising from that recomputation be forgiven. Accordingly, deferred taxes previously provided were eliminated, and a one-time $14 million credit was recognized in 1984.*

A young, active family requires lots of athletic apparel and equipment. For the young, this apparel serves as the proper attire for all but the most formal of occasions, and even Mom and Dad have been known to wear warm-up suits when they have friends over for a casual Sunday brunch. National brand names are the foundation of sports equipment offered by JCPenney.

Home and hearth—the center of so much of today's family-oriented lifestyle. Approximately 46 per cent of young marrieds, ages 20 to 29, own their own home, and they're spending time and money to make it suit their needs and dreams.

In addition to the merchandise offered in JCPenney stores and catalog, JCPenney Custom Decorating Services, located in 430 stores servicing major markets, provide an opportunity to customers, young and old, for personal in-home service. Our decorator consultants coordinate carpeting and custom window products and assist with the overall interior design concept.

In this photo, the jacquard print sofas are by Lane, and the tea table and small chest are by Broyhill, both of which have been making furniture in America for JCPenney for many years. The fireplace is available through the catalog; the pharmacy lamp is by Steiffel, the tri candle lamp by Robert Abbey; and the Martha Washington style chair in the foreground is by Treadline. The painted, diamond-patterned floor and the fabric walls are custom touches that, though tricky to execute, add much more than their cost in style.

Insurance companies' balance sheet (In millions)	December 31 1985	1984	1983
Assets			
Investments			
Fixed income, at amortized cost (market: $308, $275, and $269)	**$294**	$281	$279
Short term, at cost which equals market	**65**	65	43
Equity, at market (cost: $108, $83, and $69)	**114**	77	73
Other	**10**	10	10
Total investments	**483**	433	405
Deferred policy acquisition costs	**195**	179	154
Other assets	**168**	123	82
	$846	$735	$641
Liabilities and equity			
Policy and claims reserves	**$396**	$295	$239
Income taxes and other liabilities	**114**	102	98
Equity of JCPenney	**336**	338	304
	$846	$735	$641

JCP Realty, Inc. is engaged in the development and operation of real estate, principally shopping centers, through participation in joint ventures.

At year end, JCP Realty had interests in over 60 projects, primarily regional shopping centers, in various stages of development, 41 of which were in operation.

JCP Realty recorded profits of $22 million, $6 million, and $5 million in each of the last three years. Included in 1985 results was an after tax gain of $19 million from sales of its partial interests in several shopping center ventures. JCP Realty has advanced to JCPenney an amount in excess of its equity as follows:

Net investment in JCP Realty, Inc. (In millions)	1985	1984	1983
Amount advanced to JCPenney	**$(88)**	$(85)	$(78)
Equity of JCPenney	**65**	43	31
Net investment of JCPenney	**$(23)**	$(42)	$(47)

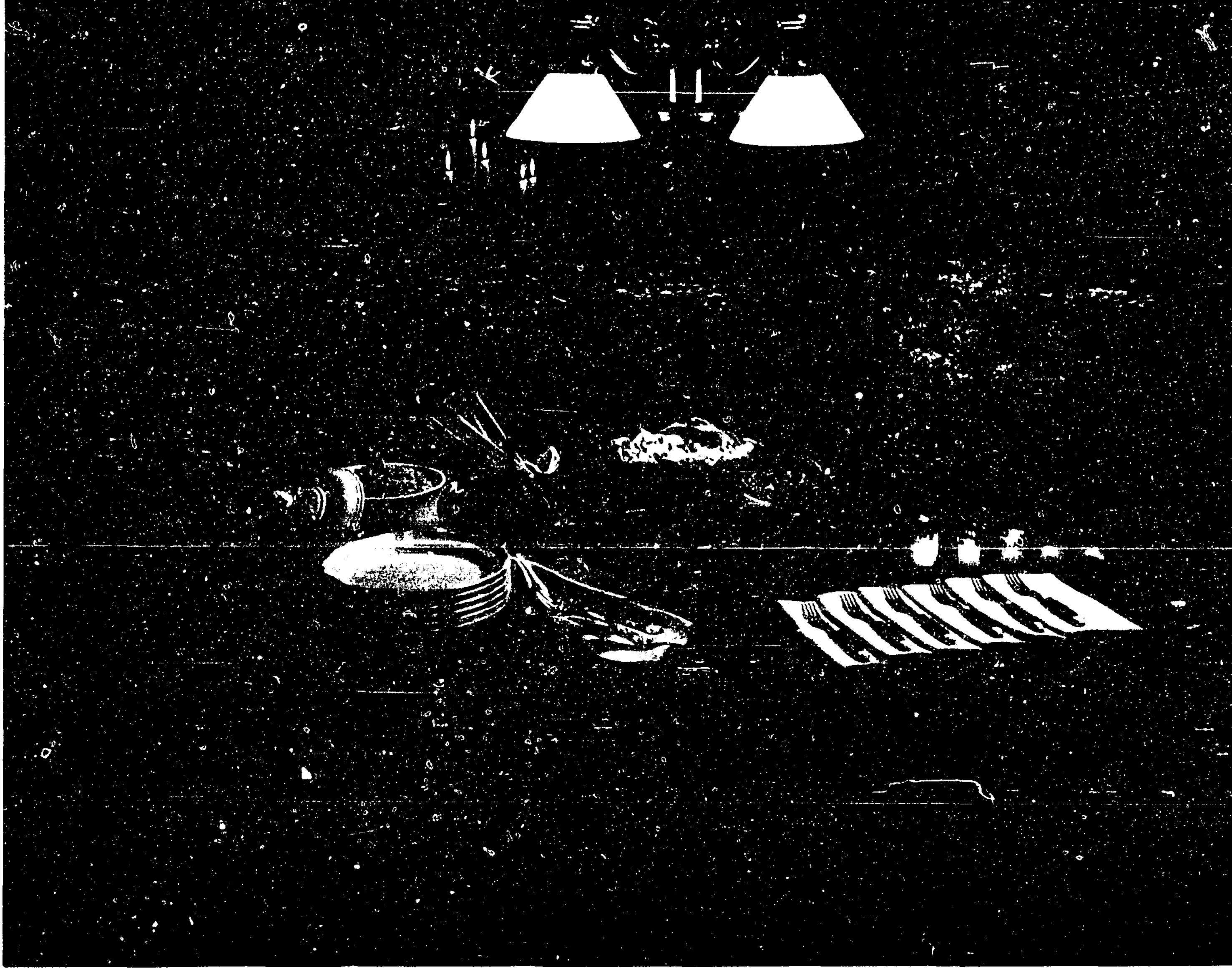
Assets

Receivables (In millions)	1985	1984	1983
Customer receivables	**$4,233**	$3,776	$3,485
Less allowance for doubtful accounts	**72**	64	70
Customer receivables, net	**4,161**	3,712	3,415
Other receivables, net	**343**	307	258
Receivables, net	**$4,504**	$4,019	$3,673

Merchandise inventories (In millions)	1985	1984	1983
Merchandise inventories, at lower of cost (FIFO) or market	**$2,516**	$2,585	$2,252
LIFO reserve	**(218)**	(202)	(259)
Merchandise inventories, at lower of cost (LIFO) or market	**$2,298**	$2,383	$1,993

Properties (In millions)	1985	1984	1983
Land	**$ 136**	$ 131	$ 135
Buildings			
Owned	**1,359**	1,232	1,167
Capital leases	**247**	251	254
Fixtures and equipment	**1,814**	1,640	1,376
Leasehold improvements	**407**	369	323
	3,963	3,623	3,255
Less accumulated depreciation and amortization	**1,151**	1,015	897
Properties, net	**$2,812**	$2,608	$2,358

JCPenney



Capital expenditures (In millions)	**1985**	1984	1983
Land	**$ 6**	$ 6	$ 3
Buildings	**121**	73	109
Fixtures and equipment	**245**	333	241
Leasehold improvements	**54**	93	90
Total capital expenditures	**$426**	$505	$443
JCPenney stores			
Modernizations	**$219**	$356	$276
New stores	**113**	81	79
	332	437	355
Other	**94**	68	88
Total	**$426**	$505	$443

Liabilities and Stockholders' Equity

Accounts payable and accrued expenses (In millions)	**1985**	1984	1983
Trade payables	**$ 424**	$ 398	$ 431
Dividend payable	**44**	44	40
Taxes, other than income taxes	**195**	180	177
Accrued salaries, vacations, profit-sharing, and bonuses	**361**	331	339
Other	**258**	192	281
Total	**$1,282**	$1,145	$1,268

Since virtually everyone is into cooking these days, what better way to demonstrate one's prowess with a whisk or a wok than when entertaining at home for fellow gourmets. A pretty setting enhances the food. Concord Manor's country dining room furniture has a soft honey pine finish and features traditional *Queen Anne styling. The solid brass* chandelier is by E.J.S.

Opposite is JCPenney's moderately priced private label stoneware called "Victorian Flowers." It is shown with "Versailles" flatware, available in seven fashion colors through the catalog.

Short term debt (In millions)	**1985**	1984	1983
Commercial paper	**$ 480**	$ 557	$ 385
Master notes and other	**260**	245	224
Short term debt	**740**	802	609
Short term investments	**(136)**	(161)	(214)
Short term debt, net	**$ 604**	$ 641	$ 395

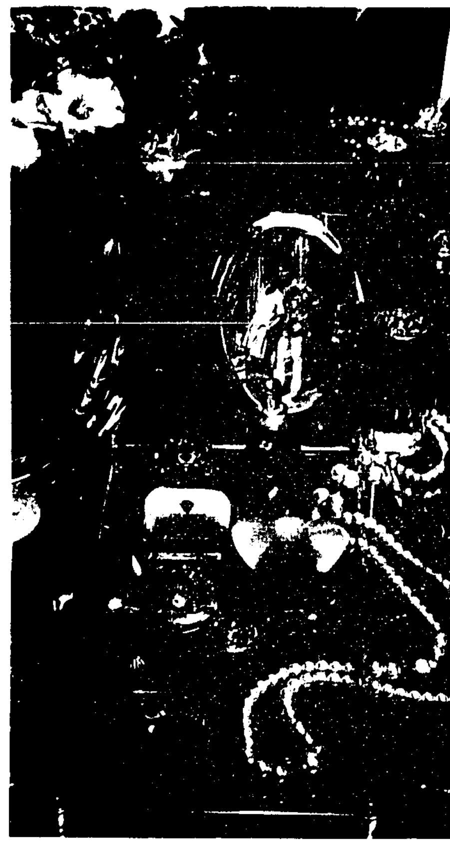
Average borrowings, investments, and interest rates	Average amounts (In millions)			Average rates		
	1985	1984	1983	**1985**	1984	1983
Short term debt	**$ 875**	$1,076	$1,046	**8.0%**	10.1%	9.1%
Short term investments	**(270)**	(398)	(451)	**(8.2)**	(10.5)	(9.4)
Short term debt, net	**605**	678	595	**7.9**	9.9	8.9
Long term debt	**2,774**	2,507	2,065	**11.3**	11.3	10.5
Total debt, net	**$3,379**	$3,185	$2,660	**10.7**	11.0	10.2

The Company's short term debt requirements normally peak before the holiday selling season. The highest balance outstanding for each of the last three years was $1.2 billion, $1.4 billion, and $1.5 billion, respectively.

Long term debt (In millions)	**1985**	1984	1983
Original issue discount			
Zero coupon notes and 6% debentures, due 1989 to 1994 and 2006, $900 at maturity, yield 13.5% to 15.1%, effective rates 12.5% to 13.5%	**$ 390**	$ 351	$ 316
Debentures and notes			
5.375% to 8.875%, due 1987 to 1998	**339**	348	358
9% to 11.875%, due 1987 to 1999	**834**	646	554
12% to 13.75%, due 1985 to 1999	**450**	550	350
11% to 12.375%, due 2010 to 2015	**650**	500	400
4.5% and 6% convertible, due 1987 and 1989	**45**	45	45
Other	**157**	161	162
	2,865	2,601	2,185
Present value of commitments under capital leases	**234**	246	255
Long term debt and commitments under capital leases	**$3,099**	$2,847	$2,440

Changes in long term debt (In millions)	**1985**	1984	1983
Increases			
6.75% Euro-yen notes, due 1992, effective rate 10.8%	**$102**	$ —	$ —
9.75% notes, due 1995	**100**	—	—
11% and 12.375% sinking fund debentures, due 2014 and 2015	**150**	100	—
11.75% to 13.75% notes, due 1987 to 1999	**—**	400	250
Amortization of original issue discount	**39**	35	30
Other, net	**(39)**	(3)	39
	352	532	319
Decreases			
Transfers to current maturities of long term debt	**—**	125	100
12.375% notes, due 1986, called in 1985	**100**	—	—
Increase in long term debt	**$252**	$407	$219

Maturities of long term debt (In millions)	Long term debt	Capital leases
1986	$ 33	$ 24
1987	226	24
1988	43	24
1989	301	23
1990	292	24
1991 to 1995	1,483	115
Thereafter	997	141
Total	$3,375	375
Less future interest and executory expenses		141
Present value		$234



In addition to a photo taken on a recent vacation, Mom's dressing table boasts four of her and JCPenney's favorite fragrances: Arpege, Albert Nipon, Gucci, and Halston.

What could be more enjoyable at the end of the day than snuggling with Mom in a bed, by Eden House, as pretty as the one in our picture. The comforter features a reproduction of an antique country stoneware pattern; sheets and shams are coordinated with it. An adorable rabbit and duck (not shown) are replicas of popular antique collectibles. The whole collection, a JCPenney exclusive, will be available through our 1986 Fall and Winter Catalog. The gown and peignoir that Mom is wearing are among the treats to be found in JCPenney's 1986 Holiday Catalog.

Confirmed lines of credit available to JCPenney amounted to $748 million. None was in use at January 25, 1986.

Stockholders' equity rose to $4,051 million at year end 1985 from $3,812 million at year end 1984 and $3,559 million at year end 1983.

In 1984, the Company increased the number of authorized shares of common stock and preferred stock to 500 million shares and 25 million shares from 100 million shares and 5 million shares, respectively. None of the preferred stock has been issued.

Rights to purchase preferred stock. On January 28, 1986, the Company declared a dividend distribution of one preferred stock purchase right on each outstanding share of common stock, payable as of February 7, 1986 to stockholders of record on that date.

The rights will not become exercisable until the close of business ten days after a public announcement that a person or group has acquired 20 per cent or more of the Company's common stock or a public announcement or commencement of a tender or exchange offer which would result in a person or group acquiring 30 per cent or more of the Company's common stock. Once exercisable, each right would entitle stockholders to buy $\frac{1}{100}$ of a share of Series A Junior Participating Preferred Stock at an exercise price of $150. The Company authorized 1.6 million shares of the Series A Preferred Stock.

If the Company is acquired in a merger or other business combination transaction, each right then exercisable will entitle its holder to purchase that number of shares of the acquiring company's common stock which has a market value equal to twice the right's exercise price. In addition, if the Company were to be the surviving corporation in a merger or other business combination transaction with a 20 per cent stockholder, or such stockholder were to engage in certain self-dealing transactions with or through the Company, each right (other than rights owned by the 20 per cent holder, which will thereupon become null and void) will entitle its holder to purchase that number of shares of the Series A Preferred Stock which has a market value equal to twice the right's exercise price. The Company may redeem the rights for 10 cents per right prior to the close of business on the tenth day after a public announcement that 20 per cent or more of the Company's common stock has been acquired by a person or group. The rights will expire on February 7, 1996, unless redeemed at an earlier date.

1984 Equity Compensation Plan and Performance Unit Plan. Under the 1984 equity compensation plan, 1.2 million shares of common stock, as well as 1.5 million shares available under a previous stock option plan, were initially reserved for issuance upon the exercise of stock options or related stock appreciation rights (SARs) and for payment of stock awards. At year end 1985, 2.4 million shares remained in reserve and were available for grant. Under this plan, ten-year incentive stock options, non-qualified stock options, and SARs and tax benefit rights (TBRs) in tandem with stock options may be granted. Options generally become exercisable one year from date of grant.

In 1985, 1984, and 1983, the Company granted SARs and in 1985 and 1984, TBRs, to officers in tandem with certain stock option grants. With respect to SARs and TBRs, less than $1 million was paid to participants in each of the three years.

Under the 1984 performance unit plan, performance units are earned based on measurements of Company performance determined by the Personnel and Compensation Committee of the Board of Directors. For 1985, 1984, and 1983, under this plan and a previous performance unit plan, approximately $5 million was earned in each of the last three years. Beginning in 1985, performance unit plan payments may be deferred by participants.

	1985		1984		1983	
Stock options	Shares (In thousands)	Option price	Shares (In thousands)	Option price	Shares (In thousands)	Option price
Balance at beginning of year	**1,644**	**$24.44-59.75**	1,625	$24.44-70.44	2,267	$24.44-70.44
Granted	**294**	**48.00-49.81**	246	51.94	210	58.44-59.75
Exercised	**(216)**	**24.44-51.94**	(133)	24.44-51.50	(793)	24.44-58.82
Expired and cancelled	**(185)**	**29.38-58.82**	(94)	29.38-70.44	(59)	24.44-70.44
Balance at end of year	**1,537**	**$24.44-59.75**	1,644	$24.44-59.75	1,625	$24.44-70.44

The quarterly dividend was 59 cents per share in 1985 and 1984, and 54 cents per share in 1983, or an annual rate of $2.36 per share in 1985 and 1984, compared with $2.16 in 1983. Dividends were $176 million in 1985, $175 million in 1984, and $160 million in 1983.

Changes in outstanding common stock	Shares (In thousands)			Amounts (In millions)		
	1985	1984	1983	**1985**	1984	1983
Balance at beginning of year	**74,371**	74,247	73,453	**$922**	$919	$892
Common stock issued, primarily options exercised	**206**	124	794	**7**	3	27
Balance at end of year	**74,577**	74,371	74,247	**$929**	$922	$919

A career Mom can easily create a glamorous image for a well deserved night on the town. Starting with JCPenney's sequinned tunic top and black silk pants, she completes the look with diamond stud earrings, a diamond and ruby bangle, and a splash of Arpege.

There were approximately 66 thousand stockholders of record at year end 1985. One of these stockholders was the savings and profit-sharing retirement plan which had 123 thousand participants and held 11.8 million shares of the Company's common stock at year end 1985, representing about 16 per cent of the shares outstanding.

Additional Financial Data

Sales through JCPenney, Visa, MasterCard, and American Express cards were as follows:

Credit sales	1985 Amounts (In billions)	1985 Per cent of eligible sales	1984 Amounts (In billions)	1984 Per cent of eligible sales	1983 Amounts (In billions)	1983 Per cent of eligible sales
JCPenney credit card	**$6.5**	**49.2**	$5.9	45.7	$5.1	44.0
Other credit cards	**1.1**	**8.2**	1.0	7.4	.7	5.9
Total	**$7.6**	**57.4**	$6.9	53.1	$5.8	49.9

Eligible sales exclude sales in Belgium.

Approximately 86 per cent of sales on the JCPenney credit card was made in accordance with the regular plan and the balance in accordance with the major purchase plan.

At year end, the number of JCPenney credit accounts with outstanding balances was 15.4 million under the regular plan and 2.2 million under the major purchase plan.

Average balances and maturities	Average account balances 1985	1984	1983	Average maturities (In months) 1985	1984	1983
Regular plan	**$200**	$194	$185	**4.5**	4.4	4.7
Major purchase plan	**$503**	$470	$434	**10.8**	11.9	12.1
All	**$238**	$229	$218	**5.3**	5.4	5.8

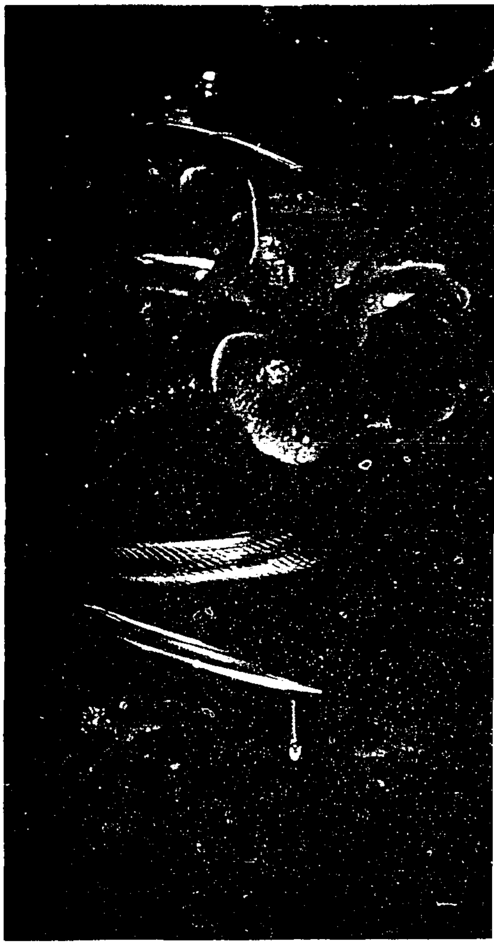
Key credit information (In millions)	1985	1984	1983
Customer receivables			
Regular plan	**$3,122**	$2,792	$2,560
Major purchase plan	**1,111**	984	925
Total customer receivables	**$4,233**	$3,776	$3,485
Number of accounts with balances	**17.6**	16.5	15.9
Finance charge revenue	**$ 671**	$ 587	$ 569
Net bad debts written off	**$ 101**	$ 71	$ 81
Per cent of customer charges	**1.4**	1.1	1.5
Provision for doubtful accounts	**$ 109**	$ 65	$ 82
Accounts 90 days or more past due as a per cent of customer receivables	**2.1**	1.8	2.0

The Company's policy is to write off accounts when the scheduled minimum payment has not been received for six consecutive months, or if any portion of the balance is more than 12 months past due, or if it is otherwise determined that the customer is unable to pay. Collection efforts continue subsequent to write off, and recoveries are applied as a reduction of bad debt losses.

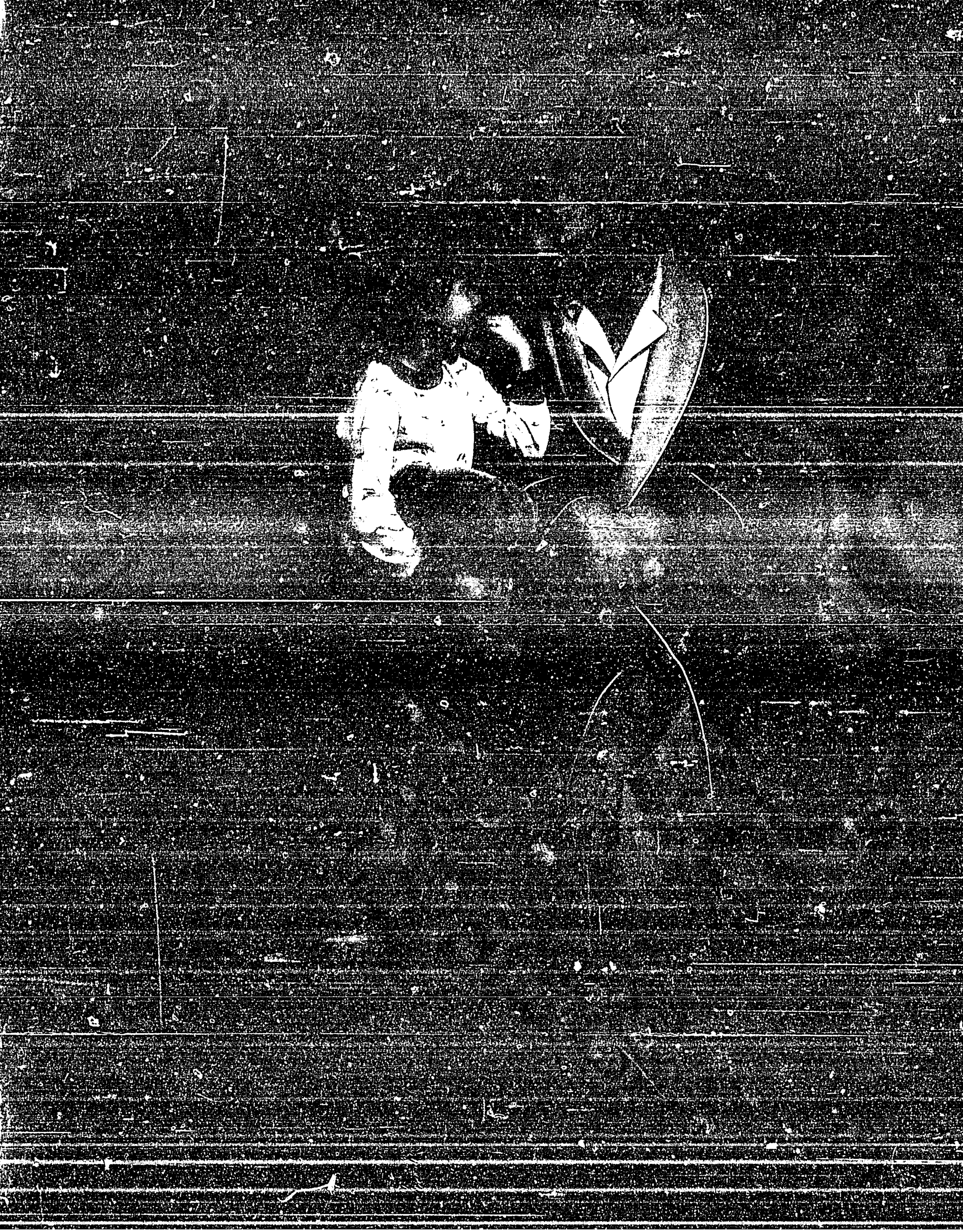
Electronic communications network. The Company has been marketing to other companies the use of its nationwide electronic communications network to provide credit authorization, processing, data capture capabilities, and other services. Major industries served cover petroleum, retailing, and banking, and customers include Shell, Chevron/Gulf, Zale, Zions First National Bank, and Citgo/7-Eleven locations.

Advertising expense by the Company for newspapers, television, radio, and other media, excluding catalog preparation and distribution costs, was $442 million in 1985, as compared with $465 million in 1984 and $381 million in 1983.

Interest expense (In millions)	1985	1984	1983
Short term debt	**$ 70**	$108	$ 95
Income on short term investments	**(22)**	(41)	(42)
Short term debt, net	**48**	67	53
Long term debt	**313**	282	217
Capitalized	**(5)**	(7)	(2)
Capital leases and other	**14**	8	(2)
Interest expense, net	**$370**	$350	$266



Over the past year, sales of fine jewelry have been consistently strong, with diamond stud earrings and gold bangles among the items most in demand. Our success with this type of merchandise, as well as with cosmetics and fragrances, all of which are so-called ego sensitive, testifies to the strides we have made in our repositioning efforts.



Rent expense (In millions)	**1985**	1984	1983
Minimum rent on noncancellable operating leases	**$195**	$192	$194
Rent based on sales	**45**	45	45
Minimum rent on cancellable personal property leases	**113**	80	57
Real estate taxes and common area costs	**82**	73	73
Total	**$435**	$390	$369

The Company conducts the major part of its operations from leased premises which include retail stores, distribution centers, warehouses, offices, and other facilities. Almost all leases will expire during the next 25 years; however, most leases will be renewed or replaced by leases on other premises.

Minimum annual rents under noncancellable leases and subleases (In millions)	Gross rents	Net rents*
1986	$ 193	$ 130
1987	181	121
1988	166	108
1989	158	101
1990	148	95
Thereafter	1,602	1,104
Total	$2,448	$1,659
Present value		$ 800
Weighted average interest rate		10%

**Rents are shown net of their estimated executory costs which are principally real estate taxes, maintenance, and insurance*

Retirement plans (In millions)	**1985**	1984	1983
Pension expense (credit)	**$ (4)**	$26	$35
Savings and profit-sharing expense	**40**	37	42
Total	**$36**	$63	$77

JCPenney's principal pension plan, which is noncontributory, covers substantially all United States employees who have completed 1,000 or more hours of service within a period of 12 consecutive months. In addition, the Company has an unfunded, noncontributory, supplemental retirement program for certain management employees.

Benefits under the principal pension plan are 1.5 per cent of final average pay for each year of credited service to normal retirement age up to a maximum of 30 years, less up to 50 per cent of an employee's estimated Social Security benefit, as computed under the plan. The actuarial method used by the Company is the projected unit credit method. The assumed rate of return used in determining pension expense was increased to 9.5 per cent for 1985 from 8.5 per cent used in the previous two years. Plan assets reflect current market values.

The decrease in 1985 pension expense was attributable equally to revisions in the assumed rate of return as well as strong investment performance. The increase in investment return reflects long term expectations for future growth in pension plan assets.

The actuarial method and assumptions used by the Company for the supplemental retirement program were the same as in the principal pension plan except that the Company's incremental borrowing rate was used in the calculations.

The present value of accumulated benefits and actuarial liability for all participants in the Company's principal pension plan and the supplemental retirement program and the net assets of the principal pension plan were as follows:

	December 31		
Pension benefits data (In millions)	**1985**	1984	1983
Present value of accumulated benefits			
Vested	**$486**	$435	$383
Non-vested	**30**	36	39
	$516	$471	$422
Present value of actuarial liability	**$627**	$678	$628
Net assets available for benefits	**$903**	$737	$735

The present value of accumulated benefits shown above is based on compensation and service to date. The present value of actuarial liability considers estimates of future compensation, but not future service, and is used to determine pension expense and funding. No contribution was required or made for 1985 or 1984.

The savings and profit-sharing retirement plan encourages savings by employees through the allocation of 4.5 per cent of the Company's available profits, as defined in the plan, to participants who make deposits under the plan. The eligibility requirement is the same as that of the Company's principal pension plan.

Every little boy and girl needs a teddy to help them bear the vicissitudes of their young lives—some even refuse to be parted in adulthood. No wonder plush toys are an area of concentration, within the toy category, for JCPenney.

Every Dad needs a small wing chair like the one on the opposite page, custom covered in plaid by Lane, that can be drawn up to his desk once good nights have been said and the last secrets of the day have been shared.

JCPenney

The Company contributed approximately $9 million, $8 million, and $8 million in 1985, 1984, and 1983, respectively, to the savings and profit-sharing retirement plan under the Employee Stock Ownership feature of the Internal Revenue Code. The contribution is invested in Company common stock and allocated equally among all eligible employees. The amount of the contribution reduces Federal income taxes otherwise payable.

The Company provides post-retirement health care benefits to retired employees and their dependents meeting certain eligibility requirements. The Company recorded expenses for these benefits as incurred in the amounts of $7 million, $7 million, and $5 million in 1985, 1984, and 1983, respectively.

Retirement plans' net assets at market value (In millions)	Savings and profit-sharing December 31 **1985**	1984	1983	Pension December 31 **1985**	1984	1983
JCPenney common stock (12 million shares at cost: $500, $505, and $459)	**$ 663**	$569	$657	**$ —**	$ —	$ —
Funds with insurance companies	**391**	290	238	**—**	—	—
Equity securities (cost: $20, $18, $16, $521, $420, and $349)	**36**	26	22	**624**	445	432
Fixed income investments (cost: $3, $5, $6, $173, $203, and $225)	**3**	5	6	**181**	205	224
Other investments (cost: $81, $66, and $56)	**—**	—	—	**98**	81	69
Other assets, net	**50**	32	36	**—**	6	10
Net assets	**$1,143**	$922	$959	**$903**	$737	$735

Changes in retirement plans' net assets (In millions)	Savings and profit-sharing December 31 **1985**	1984	1983	Pension December 31 **1985**	1984	1983
Net assets at beginning of year	**$ 922**	$ 959	$ 818	**$737**	$735	$591
Company contribution	**40**	37	42	**—**	—	28
Participants' contributions	**102**	93	84	**—**	—	—
Investment income	**70**	57	48	**97**	73	97
Unrealized appreciation (depreciation) of investments	**116**	(118)	92	**86**	(53)	32
Benefits paid	**(107)**	(106)	(125)	**(17)**	(18)	(13)
Net assets at end of year	**$1,143**	$ 922	$ 959	**$903**	$737	$735

Income tax expense (In millions)	**1985**	1984	1983
Current			
Federal	**$ 76**	$100	$216
State and local	**8**	13	17
	84	113	233
Deferred			
Federal	**187**	155	86
State and local	**26**	22	26
	213	177	112
Total income tax expense	**$297**	$290	$345
Effective tax rate	**43.5%**	41.7%	44.0%

Current income tax expense includes the net change in the current portion of deferred income taxes.

Reconciliation of tax rates	Amounts (In millions) **1985**	1984	1983	Per cent of pre-tax income **1985**	1984	1983
Federal income tax statutory rate	**$314**	$321	$362	**46.0**	46.0	46.0
Investment tax credits	**(26)**	(28)	(25)	**(3.7)**	(4.0)	(3.2)
State and local income taxes, less Federal income tax benefit	**18**	19	23	**2.7**	2.7	2.9
Employee stock ownership plan credits	**(9)**	(8)	(8)	**(1.3)**	(1.1)	(.9)
Capital gains benefits and other	**—**	(14)	(7)	**(.2)**	(1.9)	(.8)
Total income tax expense	**$297**	$290	$345	**43.5**	41.7	44.0

Traditionally, soft home furnishings have been a significant part of JCPenney's merchandise mix. This remains true, but what has changed over the years is that the emphasis in building these lines has switched from the mainly utilitarian, such as the white cotton bed sheet, to merchandise that is fashionable, easy care, full of pattern and color.

With JCPenney stores and catalog offering complementary assortments, customers have a broad spectrum from which to choose. This fact, coupled with our reputation for exceptional quality and good prices, explains why we're the dominant retailer in a number of soft home categories.

JCPenney

The Company acquired certain assets under leveraged lease arrangements and purchased tax benefits under the provisions of the Economic Recovery Tax Act. For income tax purposes, the Company received certain income tax deductions and credits that were used to reduce income taxes otherwise payable. Deferred taxes were provided to reflect the reversal of these tax benefits in future years.

Taxes other than income taxes, over half of which were payroll taxes, totaled $295 million in 1985, up from $263 million in 1984 and $254 million in 1983.

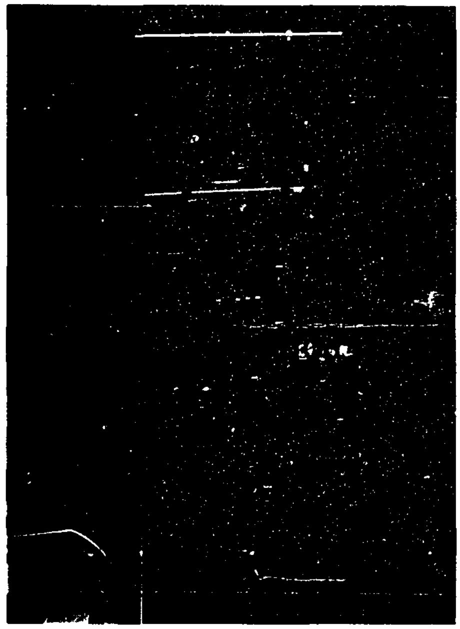
Quarterly Data (Unaudited)	First			Second			Third			Fourth		
(In millions except per share data)	**1985**	1984	1983	**985**	1984	1983	**1985**	1984	1983	**1985**	1984	1983
Sales	**$2,802**	2,752	2,379	**3,014**	3,058	2,616	**3,245**	3,211	2,914	**4,686**	4,430	4,169
Per cent increase (decrease) from prior year	**1.8**	15.7	1.7	**(1.4)**	16.9	3.1	**1.1**	10.2	5.4	**5.8**	6.3	10.5
Gross margin, per cent of sales	**33.7**	34.1	33.2	**31.2**	32.1	32.0	**34.2**	34.8	34.0	**32.3**	31.3	33.7
Selling, general, and administrative expenses, per cent of sales	**27.4**	27.1	26.9	**26.7**	26.7	26.3	**26.3**	26.5	26.1	**22.0**	21.7	21.2
Net income	**$ 50**	69	58	**30**	49	55	**93**	101	94	**224**	216	260
Per cent increase (decrease) from prior year	**(26.6)**	18.6	4.9	**(40.4)**	(10.7)	(9.9)	**(7.4)**	6.6	18.6	**3.8**	(16.6)	10.7
Net income per share	**$ .67**	.92	.78	**.40**	.66	.74	**1.24**	1.34	1.26	**3.00**	2.89	3.47
Dividends per share	**$ .59**	.59	.54	**.59**	.59	.54	**.59**	.59	.54	**.59**	.59	.54
Common stock price range												
High	**$ 51**	55	68	**52**	55	67	**50**	55	63	**58**	54	64
Low	**$ 46**	48	51	**46**	47	56	**46**	50	54	**48**	45	51

Five Year Financial Summary

J.C. Penney Company, Inc. and Consolidated Subsidiaries

Results for year (In millions)	**1985**	1984	1983	1982*	1981*
Sales	**$13,747**	13,451	12,078	11,414	11,369
Sales of JCPenney stores and catalog	**$12,634**	12,372	11,033	10,364	10,165
Per cent increase from prior year	**2.1**	12.1	6.5	2.0	7.2
Per cent increase in general merchandise inflation	**2.0**	1.0	2.7	2.8	4.7
Gross margin, per cent of sales	**32.8**	32.9	33.3	32.5	31.8
Selling, general, and administrative expenses, per cent of sales	**25.1**	25.1	24.6	24.2	23.9
Interest, net, per cent of sales	**2.7**	2.6	2.2	2.3	2.0
Depreciation and amortization	**$ 212**	198	153	144	150
Retail income before income taxes	**$ 683**	697	786	706	657
Per cent of sales	**5.0**	5.2	6.5	6.2	5.8
Income taxes	**$ 297**	290	345	302	295
Retail income	**$ 386**	407	441	404	362
Per cent increase (decrease) from prior year	**(5.1)**	(7.7)	9.0	11.6	43.1
Per cent of sales	**2.8**	3.0	3.7	3.5	3.2
Income from continuing operations	**$ 397**	435	467	430	393
Per cent of stockholders' equity	**10.4**	12.2	14.5	14.7	14.9
Per share					
Income from continuing operations	**$ 5.31**	5.81	6.25	5.87	5.59
Dividends	**$ 2.36**	2.36	2.16	2.00	1.84
Stockholders' equity	**$ 54.32**	51.26	47.93	43.94	40.81
Financial position (In millions)					
Receivables, net	**$ 4,504**	4,019	3,673	3,624	3,284
Merchandise inventories	**$ 2,298**	2,383	1,993	1,594	1,549
Properties, net	**$ 2,812**	2,608	2,358	1,987	1,878
Capital expenditures	**$ 426**	505	443	287	205
Total assets	**$10,522**	9,793	8,860	8,175	7,556
Total debt	**$ 3,839**	3,774	3,149	2,981	2,745
Stockholders' equity	**$ 4,051**	3,812	3,559	3,228	2,933
Number of shares outstanding at year end (In millions)	**75**	74	74	73	72
Number of employees at year end (In thousands)	**177**	180	175	173	179

**The amounts for 1982 and 1981 exclude discontinued automotive operations.*



JCPenney's MCS state-of-the-art stereo system is finding its way into more and more homes, with one factor being the fine reputation MCS has earned among audiophiles as a result of ratings accorded it by publications in the field.

The one shown here features all top-of-the-line components, including the latest in compact disc players, and is available through JCPenney stores and catalog.

Justly celebrated as well is JCPenney's line of Sesame Street apparel, now in its 11th year and still going strong. And what better way to capture both quiet moments and momentous occasions than with JCPenney's Camcorder shown on the opposite page.

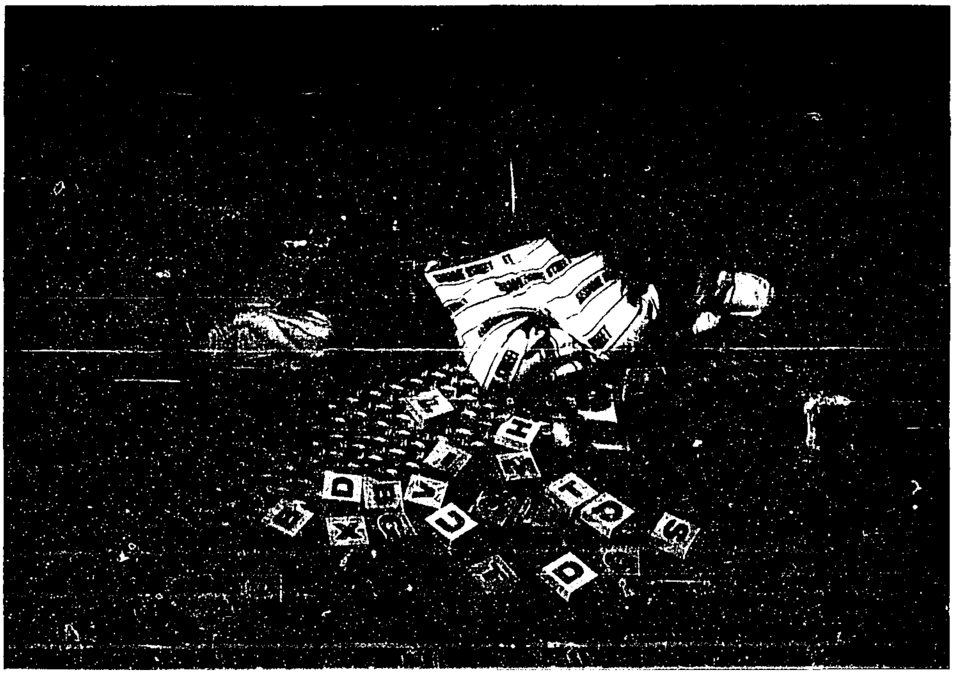
Five Year Operations Summary

J C Penney Company, Inc and Consolidated Subsidiaries

	1985	1984	1983	1982	1981
JCPenney metropolitan market department stores*					
Number of stores	**566**	565	553	540	526
Gross selling space (In million sq. ft.)	**88.8**	88.5	85.8	84.3	83.1
Sales (In millions)	**$9,524**	9,200	8,082	7,480	7,192
Sales per gross square foot	**$ 107**	106	95	89	88
JCPenney metropolitan market soft line stores*					
Number of stores	**163**	184	201	236	254
Gross selling space (In million sq. ft.)	**7.9**	8.7	9.5	10.8	11.3
Sales (In millions)	**$ 858**	893	906	948	1,047
Sales per gross square foot	**$ 103**	98	92	87	90
JCPenney geographic market stores*					
Number of stores	**753**	821	843	855	882
Gross selling space (In million sq. ft.)	**18.8**	19.2	19.0	19.0	19.1
Sales (In millions)	**$1,783**	1,820	1,637	1,536	1,559
Sales per gross square foot	**$ 93**	95	86	80	82
Catalog					
Number of sales facilities	**1,733**	1,804	1,799	1,812	1,842
Number of distribution centers	**6**	6	6	6	5
Distribution space (In million sq. ft.)	**11.4**	11.4	11.4	11.4	9.6
Sales (In millions)	**$2,000**	1,928	1,831	1,701	1,680
Drug stores					
Number of stores	**374**	369	359	353	343
Gross selling space (In million sq. ft.)	**4.0**	3.9	3.8	3.8	3.7
Sales (In millions)	**$ 702**	649	586	536	507
Sales per gross square foot	**$ 180**	170	157	147	135
Belgian stores					
Number of stores	**53**	55	58	62	72
Gross selling space (In million sq. ft.)	**3.3**	3.4	3.5	3.6	3.9
Sales (In millions)	**$ 472**	488	513	565	748
Sales per gross square foot	**$ 56**	56	62	70	98

Catalog merchandise sold through catalog sales departments located in JCPenney stores and drug stores is included in the sales of those stores, as well as in Catalog. Sales per gross square foot include only those sales from stores in operation throughout both the current and prior year.

**Restated to reflect reclassification of stores.*



Corporate Responsibility

During 1985, the Company continued to make prudent investments in the social concerns and well-being of the communities in which it does business. A policy of recognizing our obligations and seeking opportunities to meet them led to the following representative initiatives.

Charitable Contributions. The focus of Company giving programs is on health, human service, and civic betterment organizations in communities where it does business. In 1985, charitable contributions totaled $9.7 million and included $3.0 million contributed by the Company to more than 1,000 local United Ways. Over 90,000 employees throughout the country pledged an additional $4.0 million in United Way support.

Giving by local JCPenney department stores and other facilities within their communities represents the major share of our charitable support. In addition, the Company makes grants to national organizations with programs benefiting local communities as well as to those addressing nationwide concerns.

Community Programs. The Company participates in a number of programs to help improve the quality of community life.

Working with the National Association of Bank Women, the Company conducted community leadership training seminars in 29 markets during 1985. Women who are active or potential leaders in non-profit and governmental organizations participated, thus enhancing their effectiveness through improved leadership skills. The Company also sponsors leadership training for 4-H Club volunteer leaders to improve their skills in working with children. More than 1,000 4-H leaders received training in 1985.

Considerable community relations emphasis is placed on working with youth through local programs conducted with Junior Achievement, Distributive Education Clubs of America, the National School Volunteer Program, and the Hugh O'Brian Youth Foundation. Store managers and other employees represent the Company on boards and councils of these and other youth organizations, thereby furthering our involvement.

National Programs. During national Missing Children's Month in May, 1985, the Company developed and mailed "Protect Your Child" pamphlets to nearly 10 million charge account customers. These pamphlets help parents to educate children in ways of preventing abduction. Since then, more than 800,000 additional pamphlets have been distributed in response to public inquiries.

The Company also underwrote the first National Organization on Disability recognition program, which honors associations and organizations for the development of activities and policies addressing the needs of the disabled. Awardees were honored in special ceremonies last June in Washington.

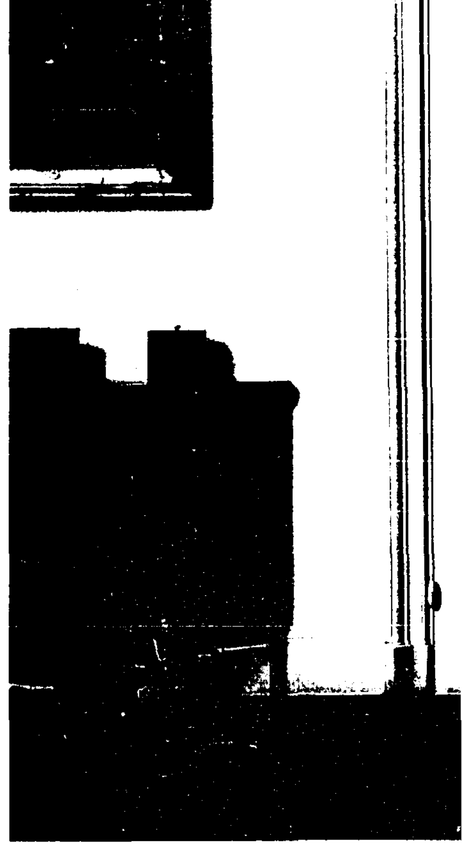
Minority Affairs. The Company has a commitment to support programs fostering equal opportunity for all. Working with the National Urban League, NAACP, League of United Latin American Citizens, United Negro College Fund, and other groups, the Company participates in scholarship programs, youth leadership development seminars, and job training programs.

As a member of the National Minority Supplier Development Council, JCPenney works with minority-owned business firms to help them become potential suppliers of goods and services. The Company was honored with national awards from the U.S. Department of Commerce and the National Minority Business Council for its efforts in 1985.

Purchases of goods and services from minority-owned businesses exceeded $122 million, representing relationships with more than 1,150 minority suppliers. Additionally, we spent $4.3 million on advertising in 119 minority media, and we maintained active accounts with 14 minority-owned banks.

Employment. The Company adheres to a policy of Equal Employment Opportunity. Year end employment totaled approximately 177 thousand, of which 168,910 were employed in the U.S., excluding unconsolidated subsidiaries. The following summary delineates minority and female representation in job categories defined in the Employment Information Report EEO-1 of the EEOC.

	Total employed		Per cent female		Per cent minority	
Employment Information	**1985**	1981	**1985**	1981	**1985**	1981
Officials, managers, and professionals	**22,350**	23,381	**44.6**	40.1	**9.1**	8.3
Management trainees	**1,122**	1,220	**56.1**	47.3	**17.9**	18.6
Sales workers	**86,800**	85,901	**86.5**	83.5	**13.4**	11.3
Office and clerical workers	**25,773**	31,059	**90.4**	92.2	**17.0**	15.1
Technicians, craft workers, and operatives	**21,722**	18,794	**81.1**	67.4	**16.6**	15.5
Laborers and service workers	**11,143**	17,343	**39.6**	40.9	**21.4**	19.3
Total	**168,910**	177,698	**77.6**	73.2	**14.4**	12.8



An early and important chapter in JCPenney's history was written while Mr. James Cash Penney and his young family lived in this house in Kemmerer, Wyoming, where he opened his first store in 1902.

Designated a national landmark in 1976, the house has been restored by the Company and is open to visitors much of the year. Volunteerism thrives in Kemmerer for the house is maintained by a citizens' group that takes special pride in the fact that their town played an important part in one aspect of American history.

Impact of Inflation on Financial Data (Unaudited)

The preceding financial information was prepared on the historical cost basis. The Financial Accounting Standards Board (FASB) has prescribed the current cost method of disclosure to address the effects of inflation on specific elements of financial statements. In accordance with the FASB's requirements, the principal adjustments to historical financial data are on property, plant, and equipment, where historical costs are increased to current costs for assets with the same service potential, and inventory, which is stated at FIFO cost.

The current cost information presented below is expressed in average 1985 dollars as measured by the CPI-U.

Five year summary of selected financial data
Adjusted for changing prices

(In millions except per share data)	1985	1984	1983	1982	1981
Sales	$13,747	13,934	13,038	12,721	13,401
Income from continuing operations	$ 374	416	458	435	423
Per share information					
Income from continuing operations	$ 5.00	5.56	6.13	5.93	6.02
Dividends	$ 2.36	2.44	2.33	2.23	2.17
Common stock price at year end	$ 55	52	56	53	35
Purchasing power gain on net monetary items	$ 61	51	47	37	101
Net assets at year end	$ 4,660	4,580	4,691	4,270	4,287
Effect of inflation on merchandise inventories and properties*	$ 215	187	117	182	378
Average CPI-U Index	323.2	312.0	299.4	290.0	274.2

**At January 25, 1986, current cost of merchandise inventories was $2,516 and current cost of properties was $3,272.*

Net income, as reported in the primary financial statements for 1985, was $397 million. After adjusting depreciation expense to reflect the increase in property, plant, and equipment on a current cost basis, net income for 1985 was $374 million. No adjustment to cost of goods sold was required since the LIFO method of inventory valuation, as reported in the primary financial statements, reflects current cost.

Net assets include property, plant, and equipment and merchandise inventories at their current cost amounts. All other items comprising net assets are as reported in the primary financial statements and have been adjusted to average 1985 dollars. For 1985, the current cost of net assets exceeded the amount reflected in the financial statements by $609 million.

Volunteerism is a uniquely American phenomenon. For many people, including our young working mother, it's part of the pattern of life. Here she serves as a guide in a private home, filled with American antiques, that the owner has graciously opened for tours by school groups and others who want to know more about their cultural heritage.

A tour guide not only needs to be smart; she needs to look smart, and Mom certainly does in this wool-blend hound's tooth jacket coordinated with black trousers.

Will the kids remember that the picture of Maria Byrd of Virginia and Child was painted circa 1820?

JCPenney

J.C. Penney Company, Inc.

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Chairman and Chief Executive Officer, Eastman Kodak Company

William M. Ellinghaus[1,4]
Executive Vice Chairman, New York Stock Exchange
Formerly President, American Telephone and Telegraph Company

Clifton C. Garvin, Jr.[1,2]
Chairman and Chief Executive Officer, Exxon Corporation

Robert B. Gill
Vice Chairman of the Board

William R. Howell
Chairman of the Board

Vernon E. Jordan, Jr.[2,4]
Partner, Law Firm of Akin, Gump, Strauss, Hauer & Feld

Juanita M. Kreps[1,4]
Economist and Educator
Formerly United States Secretary of Commerce

David B. Meeker[1,2]
Formerly Chairman of the Board, Hobart Corporation

David F. Miller
President of JCPenney Stores and Catalog

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Chancellor, Pace University

Jane C. Pfeiffer[2,3]
Independent Management Consultant

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Formerly Chairman of the Board

Joseph D. Williams
Chairman and Chief Executive Officer, Warner-Lambert Company

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Boris Yavitz[1,2]
Paul Garrett Professor of Public Policy and Business Responsibility and Former Dean, Graduate School of Business, Columbia University

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David F. Miller
President of JCPenney Stores and Catalog

Ralph B. Henderson
Executive Vice President

Thomas J. Lyons
Executive Vice President

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Robert Capone
Director of Technical Operations

Albert W. Driver, Jr.
Secretary and General Counsel

Richard T. Erickson
Director of Corporate Personnel

A. Scott Frahlich
Director of JCPenney Stores

John A. McConville
Director of Merchandise

Robert E. Northam
Chief Financial Officer

Terry S. Prindiville
Director of Corporate Marketing

Stanley J. Putman
Director of Real Estate, Construction and Corporate Services

Vice Presidents

Robert O. Amick
Controller

A. Howard Amon, Jr.
Director of Real Estate

Charles L. Brown
Director of Auditing

James P. Bryant
Director of Corporate Taxes

Joseph J. DeMelio
Director of Insurance

Thomas B. Fox
Director of European Operations

William D. Friel
Director of Systems and Data Processing

William R. Johnson
Director of Public Affairs and Company Communications

Robert J. Keller
Director of Construction Services

Donald A. McKay
Treasurer

Ted L. Spurlock
Director of Credit and Consumer Banking Services

George M. Stone
Director of Government Relations

Michael T. Todres
Director of Distribution

Regional Vice Presidents

John C. Morgenson
Southwestern Region

C. Kenneth Ogg
Western Region

Richard C. Sherwood
Eastern Region

W. Barger Tygart
Central Region

John A. Wells
Southeastern Region

Divisional Vice President

Satenig St. Marie
Director of Public Issues and Consumer Programs

Assistant Controllers

William J. Alcorn

Leo A. Gispanski

Assistant Secretaries

Frank J. Bonet

Cornelius T. Dorans

John V. Faltermeier

Margaret R. Johnson

Archibald E. King, Jr.

Richard M. Kleid

Richard P. Rubenoff

J. David Silvers

Assistant Treasurers

Robert B. Cavanaugh

John B. Hebard

1 *Member of the Audit Committee of the Board of Directors This committee recommends to the Board of Directors the inde-*pendent auditors to be employed for the purpose of conducting the annual audit of the Company's accounts, discusses with the auditors the scope of their examination, reviews the Company's financial statements and the auditors' report with Company personnel and the auditors, determines whether the auditors have received all the explanations and information they had requested, and invites the recommendations of the auditors regarding internal controls and other matters.

2 Member of the Public Affairs Committee This committee identifies, analyzes, and brings to the attention of the Board social and environmental trends and public policy issues which may have a potential impact on the business performance and investment character of the Company. It assures that Company policy and performance reflect a sensitivity toward the social and physical environments in which the Company does business and that such policy and performance are in accord with the public interest

3 Member of the Committee on Directors This committee makes recommendations to the Board with respect to the size, composition, and functions of the Board of Directors, the qualifications of directors, candidates for election as directors, and the compensation of directors

4 Member of the Personnel and Compensation Committee. This committee reviews the Company's annual and long-term incentive compensation plans, makes recommendations in areas concerning personnel relations, and takes action or makes recommendations with respect to the compensation of Company executive officers, including those who are directors It is also the committee which acts under certain of the Company's incentive compensation and retirement plans.

All of the committees described above are composed entirely of outside directors

Transfer Agents

J C Penney Company, Inc
Securityholder Services
Pittsburgh Accounting Center
P.O. Box 407
Pittsburgh, Pennsylvania 15230

Registrar and Transfer Company
61 Broadway, Room 1412
New York, New York 10006

Registrars

Registrar and Transfer Company
61 Broadway, Room 1412
New York, New York 10006

Wilmington Trust Company
Wilmington, Delaware 19899

Exchange Listings

The New York Stock Exchange
(Ticker symbol—JCP)

Brussels and Antwerp Stock Exchanges

Supplemental Information

Copies of the Company's Form 10-K annual report for 1985 to the Securities and Exchange Commission and consolidated Employer Information Reports EEO-1 for 1985 year end to the United States Equal Employment Opportunity Commission will be made available upon request to.

Ms Ann R Roberts
J.C Penney Company, Inc
Public Relations
1301 Avenue of the Americas
New York, New York 10019
Phone (212) 957-8170

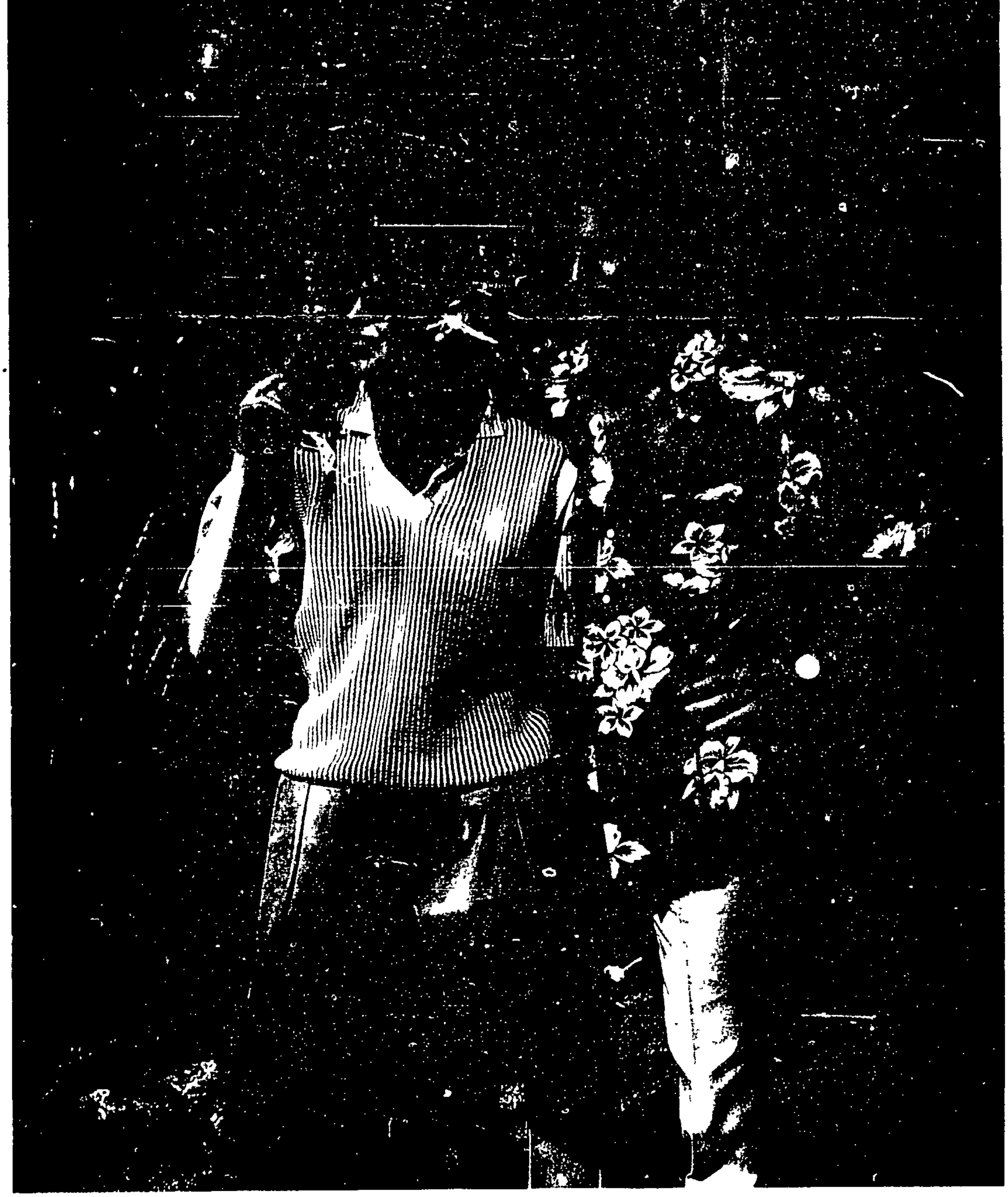
Copies of J C. Penney Financial Corporation's annual report are available from:

Mr Kelley H Mote
J C Penney Financial Corporation
P.O. Box 955
New York, New York 10116
Phone (212) 957-9244

Inquiries about your stockholder record should be forwarded to.

Mr. Alfred C Riley
J.C. Penney Company, Inc
Securityholder Services
Pittsburgh Accounting Center
P.O. Box 407
Pittsburgh, Pennsylvania 15230
Phone (412) 854-1000, Ext. 486

The old refrain about the call of far away places with strange sounding names is particularly appealing to today's young working couples who, studies show, want a life for themselves separate from their parenting role. And our young couple has taken advantage of JCPenney's exciting coordinated merchandise to help make their trip a memorable one. Her walking shorts, shown here with a cotton sweater and blouse, are right in tune with the very popular safari look. His bright colored shirt typifies one of the casual looks available in JCPenney stores right now.



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